State of Maine

Single Audit Report
Fiscal Year Ended
June 30, 1996

Prepared by
State Department of Audit
Gail M. Chase, CIA, State Auditor

STATE OF MAINE

SINGLE AUDIT REPORT

FOR THE YEAR ENDED

JUNE 30, 1996

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STATE OF MAINE

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Letter of Transmittal

To the President of the Senate and the
Speaker of the House of Representatives

Mr. John Fisher
Manager, National External Audit Review Center
U.S. Department of Health and Human Services

We are pleased to submit the Single Audit of the State of Maine as of and for the fiscal year ended June 30, 1996.

The audit, which covered over $4 billion in expenditures and of which $1.3 billion was for various Federal programs, was conducted pursuant to Title 5 MRSA §243, subsection 1, which authorizes the Department of Audit:

> To perform a postaudit of all accounts and other financial records of the state government or any department or agency thereof, including the judiciary and the Executive Department of the Governor, except the Governor's expense account, and to report annually on this audit, and at such other times as the Legislature may require.

In addition, the audit was conducted to meet the requirements of the Single Audit Act of 1984, authorized under the United States Code, USC 31, Chapter 75, and the regulations established by the U.S. Office of Management and Budget Circular A-128, *"Audits of State and Local Governments."*

The objectives of the audit were:

- To examine the State's financial statements and determine if they were presented fairly and in conformity with generally accepted accounting principles;

- To assess whether the State's systems and procedures for financial accounting, reporting and internal controls were adequate;

- To assess the State's accountability for revenues; to determine the propriety of expenditures, the extent to which funds have been expended in accordance with prescribed State and Federal laws and regulations; and to examine the State's compliance with Federal regulations pertaining to financial reports and claims for reimbursements; and

- To recommend corrective actions for any deficiencies noted, and to include management's responses to our findings and recommendations.

During the course of our audit we identified certain weaknesses in the State of Maine's accounting system and procedures, and internal control structure, as well as noncompliance with rules and regulations which are described in more detail in the Executive Summary on page vii.

On behalf of the Department of Audit, I would like to express my gratitude to employees throughout State government who have assisted us during the conduct of our audit and in the issuance of this report. We continue our mutual effort to improve financial reporting and accountability to the citizens of our State. As always, we will strive to provide the Governor, Legislature and the management of State Government agencies with meaningful information that will be useful in their decision making process.

We would be pleased to respond to any questions or comments about the 1996 Single Audit of the State of Maine.

Respectfully submitted,

Gail M. Chase, CIA
State Auditor

July 31, 1997

EXECUTIVE SUMMARY

Introduction

The *Single Audit of the State of Maine* is a financial and compliance audit which fulfills State and Federal requirements. The audit is of the primary government of the State of Maine and includes all funds, organizations, institutions, agencies, departments, and offices that are not legally separate. To satisfy the needs of the various report users, the work done results in eight individual reports, as well as a separately issued management letter. These include audit opinions on the State's financial statements and the Schedule of Federal Financial Assistance, reports on the State's compliance with laws and regulations, and reports on the design and operation of systems of internal control. Depending on the nature of an audit finding, it may be required to be included in more than one of the various reports.

Results

In general, we found that State financial managers properly managed the funds entrusted to them. However, as further described below, we noted some weaknesses in internal control that, in our judgment, could result in errors that are material to the financial statements and not be detected timely. Except as noted in the accompanying reports, State managers complied with laws and regulations governing the use of the funds. We found no noncompliance that, in our judgment, would be material to the financial statements. We did note noncompliance with both general and specific Federal requirements that, in our judgment, was material to individual Federal programs. These issues are more fully described in the compliance reports found on pages 99 and 103. We also noted other instances of noncompliance with Federal rules and regulations that we reported in the accompanying Schedule of Findings and Questioned Costs. Other instances of noncompliance with State laws and regulations, as well as comments and suggestions that may improve internal controls, will be included in a management letter that will be issued separately.

The most significant internal control weaknesses that we identified relate to external financial reporting in compliance with Generally Accepted Accounting Principles (GAAP). Although the State has adequate controls in place to process and record transactions on its budgetary basis, we identified five areas that adversely affect the State's ability to report in accordance with GAAP. These issues are discussed in more detail in the report found on page 69. Two of these areas, capital leases and fixed assets, resulted in modifications to our audit opinion, as adequate records were not available to fairly state the associated values. The State has entered into contracts to do work in these areas that should result in their being correctly reflected on future State reports. In a related audit finding, because of ongoing problems with inadequate systems and insufficient resources for capturing and reporting fiscal information in compliance with GAAP, we recommended that the Department of Administrative and Financial Services commit additional resources to external financial reporting. The Department has indicated it will do so. We also noted a problem with the accrual of payments made via the external interface disbursement system. This necessitated an audit adjustment of $15.3 million. Lastly, we noted that Lottery information is obtained from vendor systems and is the basis for certain amounts reported on the financial statements. We recommended, and the State has contracted for, evaluations of the vendors' control systems by independent auditors. One of the two vendor system evaluations has been completed.

With regard to internal controls over Federal funds, we reported that the State did not include three major Federal programs in the Cash Management Improvement Act Agreement as required. Because the programs were not included, cash management criteria were not agreed to and therefore compliance with the Act could not be determined.

In addition to the preceding internal control deficiencies, we also identified others that, in our judgment, could adversely affect the State's ability to report financial data consistently with management's assertions. These twelve deficiencies, described in more detail in the Schedule of Reportable Conditions on page 81, involved several State agencies. We recommended that the Department of Human Services transfer $982,320 from the Other Special Revenue Fund and $823,160 from the Federal Expenditure Fund to the General Fund to compensate for errors in distributing amounts. We recommended that the Department of Labor establish reasonable allowance accounts for uncollectible taxes receivable and properly differentiate between amounts recorded as deferred revenue and revenue. We recommended that the Office of Treasurer of State provide more detail to account for the Private Trust Funds and also ensure that deposits in transit at year-end are reported in the State's accounting records. We advised the Department of Education to exercise greater oversight over the school construction program. We recommended to the Department of Administrative and Financial Services that it more closely examine year-end accruals of expenditures and accounts payable and that it review the operations of the newly established retiree health insurance program to ensure compliance with Federal regulations and proper accounting. We also recommended that the Department of Mental Health and Mental Retardation improve controls over its accounting for patient care and treatment billings.

Our examination of the State's Federal financial assistance programs resulted in questioned costs of $2,960,333. Questioned costs represent the amount of Federal financial assistance that was not spent in compliance with program rules or regulations or that was insufficiently documented for us to determine compliance. Amounts questioned may result in a State liability to the Federal government.

Conclusion

Our audit resulted in a qualified opinion and identified serious weaknesses in systems of internal control, as well as various instances of noncompliance. Of the 88 audit findings contained in the accompanying reports, 27 or 31%, were previously reported. However, we recognize that State financial managers have initiated action that should resolve many of these issues. While the nature of any audit report is inherently critical, we believe the State of Maine has improved both its financial position and its systems to ensure accountability.

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Independent Auditor's Report

To the President of the Senate and the
Speaker of the House of Representatives

We have audited the accompanying primary government financial statements of the State of Maine, as of and for the year ended June 30, 1996, as listed in the table of contents. These financial statements are the responsibility of the State of Maine's management. Our responsibility is to express an opinion on these financial statements based on our audit.

Except as discussed in the first and second succeeding paragraphs, we conducted our audit in accordance with generally accepted auditing standards; *Government Auditing Standards*, issued by the Comptroller General of the United States; and the provisions of Office of Management and Budget Circular A-128, *Audits of State and Local Governments*. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Because the State of Maine does not maintain adequate systems to identify, classify and report capital leases in conformity with generally accepted accounting principles, we were unable to form an opinion regarding the amounts at which fixed assets (stated at $48.2 million), and obligations under capital leases (stated at $0 million) are recorded in the Internal Service Fund. In addition, we were unable to form an opinion regarding the amounts at which obligations under capital leases (stated at $18.9 million) and amounts to be provided for retirement of general long-term obligations (stated at $568.8 million) are recorded in the General Long-Term Obligations Account Group.

The scope of our engagement did not include an audit of the financial statements of the preceding year sufficient to enable us to express, and we do not express, an opinion on the consistency of application of accounting principles with the preceding year for the results of its operations and the cash flows of its proprietary fund types and nonexpendable trust funds.

The primary government financial statements referred to above do not include the General Fixed Assets Account Group which should be included in order to conform with generally accepted accounting principles. The amount that should be recorded in the General Fixed Assets Account Group is not known.

A primary government is a legal entity or body politic and includes all funds, organizations, institutions, agencies, departments, and offices that are not legally separate. Such legally separate entities are referred to as component units. In our opinion, except for the effect on the financial statements of the omission described in the preceding paragraph, and the effect of such adjustments, if any, as might have been determined to be necessary had records concerning capital leases been adequate (discussed in the third preceding paragraph), the primary government financial statements referred to in the first paragraph (as included in the table of contents) present fairly, in all material respects, the financial position of the primary government of the State of Maine, as of June 30, 1996, and the results of its operations and the cash flows of its proprietary fund types and nonexpendable trust funds for the year then ended in conformity with generally accepted accounting principles.

However, the primary government financial statements, because they do not include the financial data of component units of the State of Maine, do not purport to, and do not, present fairly the financial position of the State of Maine, as of June 30, 1996, and the results of its operations and the cash flows of its proprietary fund types and nonexpendable trust funds for the year then ended in conformity with generally accepted accounting principles.

The State of Maine has not presented 10-year revenue and claims development information for the state-administered public entity risk pool or 10-year historical pension information that the Governmental Accounting Standards Board has determined are necessary to supplement, although not required to be part of, the primary government financial statements.

As discussed in Note 1 to the primary government financial statements, the State of Maine has changed its method of accounting for certain tax revenues, construction in progress and workers' compensation claims in the financial statements for the fiscal year ended June 30, 1996.

As discussed in Note 1 to the primary government financial statements, the State of Maine transferred administration of the post retirement health care benefits program from a component unit to an Internal Service Fund.

In accordance with *Government Auditing Standards*, we have also issued a report dated March 31, 1997, on our consideration of the State of Maine's internal control structure and a report dated March 31, 1997 on its compliance with laws and regulations.

As described in Note 19 to the financial statements, General Fund fund balance has been restated.

Gail M. Chase
State Auditor

March 31, 1997

STATE OF MAINE
PRIMARY GOVERNMENT
COMBINED BALANCE SHEET

ALL FUND TYPES AND ACCOUNT GROUPS

June 30, 1996
(Dollars in Thousands)

	Governmental Fund Types		
	General	**Special Revenue**	**Capital Projects**
ASSETS AND OTHER DEBITS			
Cash and Short-term Investments	$40,055	$105,352	$63,650
Cash with Fiscal Agent	22,512	3,818	-
Investments	-	-	-
Restricted Deposits	10,606	-	-
Investments of Deferred Compensation Plan	-	-	-
Assets Held in Trust	-	-	-
Unemployment Deposits with US Treasury	-	-	-
Receivables (net of allowance for uncollectibles)			
Taxes	192,188	57,357	-
Due from Other Governments	-	109,694	-
Loans	-	1,468	-
Other Receivables	32,023	39,348	-
Due from Other Funds	2,949	8,703	-
Inventories	-	21,851	-
Working Capital Advances Receivable	2,086	13,217	-
Fixed Assets (net of accumulated depreciation)	-	-	-
Other Assets	1,080	95	-
Amount to be Provided for Retirement of General Long-term Obligations	-	-	-
TOTAL ASSETS AND OTHER DEBITS	$303,499	$360,903	$63,650
LIABILITIES, FUND EQUITY AND OTHER CREDITS			
LIABILITIES			
Accounts Payable	$29,023	$146,949	$3,645
Accrued Payroll	10,654	13,932	-
Compensated Absences	1,612	1,949	-
Due to Other Funds	11,621	5,157	-
Due to Other Governments	37,328	11,778	-
Deferred Revenue	73,323	21,467	-
Tax Refunds Payable	55,200	-	-
Lottery Prizes Payable	-	-	-
Loans Payable	-	-	-
Deferred Compensation Payable	-	-	-
Cer ificates of Par icipation and Other Financing Arrangements	-	-	-
Obligations Under Capital Leases	-	-	-
Agency Liabilities	-	-	-
Claims Payable	-	-	-
Other Accrued Liabilities	44,978	4,971	-
Bonds and Notes Payable	-	-	-
Working Capital Advances Payable	-	1,000	-
TOTAL LIABILITIES	263,739	207,203	3,645
FUND EQUITY AND OTHER CREDITS			
Contributed Capital	-	-	-
Retained Earnings (deficits)	-	-	-
Fund Balances (deficits):			
Reserved for Continuing Appropriations	62,984	204,910	8,297
Reserved for Nonexpendable Trusts	-	-	-
Reserved for Unemployment Benefits	-	-	-
Reserved for Debt Service	22,512	32,977	-
Reserved for Capital Projects	-	-	51,708
Other Reservations	10,971	13,182	-
Unreserved and Undesignated	(56,707)	(97,369)	-
TOTAL FUND EQUITY (deficit) AND OTHER CREDITS	39,760	153,700	60,005
TOTAL LIABILITIES, FUND EQUITY AND OTHER CREDITS	$303,499	$360,903	$63,650

See accompanying Notes to the Financial Statements.

Proprietary Fund Types		Fiduciary Fund Types	Account Group	
Enterprise	**Internal Service**	**Trust and Agency**	**General Long-term Obligations**	**TOTAL (MEMORANDUM ONLY)**
$10,462	$22,329	$75,606	$ -	$317,454
-	671	1	-	27,002
-	-	39,682	-	39,682
-	-	-	-	10,606
-	-	111,443	-	111,443
-	-	38,265	-	38,265
-	-	101,797	-	101,797
-	-	-	-	249,545
-	-	-	-	109,694
9,873	-	-	-	11,341
9,867	499	2,132	-	83,869
13	8,479	13	-	20,157
3,285	5,146	-	-	30,282
-	-	-	-	15,303
53,597	48,206	-	-	101,803
636	157	13	-	1,981
-	-	-	568,766	568,766
$87,733	$85,487	$368,952	$568,766	$1,838,990
$6,145	$4,304	$13,027	$ -	$203,093
363	930	-	-	25,879
477	985	-	26,112	31,135
1,603	1,776	-	-	20,157
-	-	-	-	49,106
351	1,088	2,120	-	98,349
-	-	-	-	55,200
7,518	-	-	-	7,518
1,731	-	-	-	1,731
-	-	111,443	-	111,443
-	22,885	-	8,045	30,930
-	-	-	18,919	18,919
-	-	95,851	-	95,851
306	52,379	-	-	52,685
725	459	1,444	-	52,577
-	-	-	515,690	515,690
1,000	13,303	-	-	15,303
20,219	98,109	223,885	568,766	1,385,566
55,861	4,941	-	-	60,802
11,653	(17,563)	-	-	(5,910)
-	-	-	-	276,191
-	-	12,152	-	12,152
-	-	100,144	-	100,144
-	-	-	-	55,489
-	-	-	-	51,708
-	-	-	-	24,153
-	-	32,771	-	(121,305)
67,514	(12,622)	145,067	-	453,424
$87,733	$85,487	$368,952	$568,766	$1,838,990

STATE OF MAINE
PRIMARY GOVERNMENT
COMBINED STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES

ALL GOVERNMENTAL FUND TYPES AND EXPENDABLE TRUST FUNDS

For the Year Ended June 30, 1996
(Dollars in Thousands)

	Governmental Fund Types			Fiduciary Fund Type
	General	**Special Revenue**	**Capital Projects**	**Expendable Trusts**
REVENUES				
Taxes	$1,614,346	$360,862	$ -	$120,876
Assessments and Other Revenue Sources	44,235	103,535	-	349
Federal Grants and Reimbursements	16,767	1,387,414	-	-
Service Charges	29,138	84,339	-	-
Miscellaneous Revenue	20,474	28,464	2,388	11,921
TOTAL REVENUES	1,724,960	1,964,614	2,388	133,146
EXPENDITURES				
General Government	133,847	122,826	555	116,836
Economic Development	27,643	63,686	2,000	-
Education and Culture	869,132	105,065	5,126	-
Human Services	524,284	1,169,889	6,299	-
Labor	4,308	50,343	-	-
Natural Resources	37,564	45,703	26,899	1,050
Public Protection	11,304	45,429	558	-
Transportation	2,765	320,852	18,516	-
Debt Service				
Principal Payments	59,575	17,510	-	-
Interest Payments	26,925	7,815	-	-
TOTAL EXPENDITURES	1,697,347	1,949,118	59,953	117,886
REVENUES OVER (under) EXPENDITURES	27,613	15,496	(57,565)	15,260
OTHER FINANCING SOURCES (uses)				
Operating Transfers In (out)	74,004	(7,048)	(3,737)	(2,508)
Bond Proceeds	-	-	76,700	-
NET OTHER FINANCING SOURCES (uses)	74,004	(7,048)	72,963	(2,508)
EXCESS OF REVENUES AND OTHER SOURCES OVER (under) EXPENDITURES AND OTHER USES	101,617	8,448	15,398	12,752
FUND BALANCES (deficits) AT July 1, 1995, AS RESTATED	(121,735)	135,005	44,607	119,959
Add: Adjustment for the Cumulative Effect on Prior Years for Change to a Different Revenue Recognition Method	59,100	10,247	-	-
FUND BALANCES (deficits) AT July 1, 1995, AS ADJUSTED	(62,635)	145,252	44,607	119,959
EQUITY TRANSFER	778	-	-	-
FUND BALANCES (deficits) AT June 30, 1996	$39,760	$153,700	$60,005	$132,711

See accompanying Notes to the Financial Statements.

STATE OF MAINE
PRIMARY GOVERNMENT
COMBINED STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES

BUDGET TO ACTUAL (NON-GAAP BUDGETARY BASIS)

GENERAL AND SPECIAL REVENUE FUND TYPES

For the Year Ended June 30, 1996
(Dollars in Thousands)

	General Fund			Special Revenue Fund		
	Actual	Budget	Variance Favorable/ (Unfavorable)	Actual	Budget	Variance Favorable/ (Unfavorable)
REVENUES						
Taxes	$1,593,186	$1,554,874	$38,312	$250,344	$249,597	$747
Fines, Forfeitures and Penalties	20,027	22,441	(2,414)	5,376	4,125	1,251
Licenses and Fees	29,746	30,045	(299)	229,879	225,553	4,326
Income from Investments	8,512	2,990	5,522	3,915	2,461	1,454
Federal grants and reimbursements	16,767	19,097	(2,330)	1,152,053	1,394,817	(242,764)
Service Charges	20,235	21,575	(1,340)	84,565	127,679	(43,114)
Miscellaneous Revenues	2,054	874	1,180	69,003	95,144	(26,141)
TOTAL REVENUES	1,690,527	1,651,896	38,631	1,795,135	2,099,376	(304,241)
EXPENDITURES						
General Government	224,279	229,441	5,162	118,885	140,943	22,058
Economic Development	27,643	31,997	4,354	63,686	96,063	32,377
Education and Culture	868,287	868,064	(223)	101,453	97,069	(4,384)
Human Services	506,056	549,455	43,399	1,048,962	1,139,625	90,663
Labor	4,308	14,387	10,079	50,343	110,141	59,798
Natural Resources	37,564	38,908	1,344	45,703	76,268	30,565
Public Protection	11,304	12,282	978	45,429	57,569	12,140
Transportation	2,765	3,006	241	334,198	415,751	81,553
TOTAL EXPENDITURES	1,682,206	1,747,540	65,334	1,808,659	2,133,429	324,770
EXCESS (deficiency) OF REVENUES OVER (under) EXPENDITURES	8,321	(95,644)	103,965	(13,524)	(34,053)	20,529
OTHER FINANCING SOURCES (uses)						
Operating Transfers In (out)	75,875	83,277	(7,402)	3,791	28,086	(24,295)
Other	(8,257)	-	(8,257)	(903)	-	(903)
TOTAL OTHER FINANCING SOURCES (uses)	67,618	83,277	(15,659)	2,888	28,086	(25,198)
EXCESS (deficiency) OF REVENUES AND OTHER FINANCING SOURCES OVER (under) EXPENDITURES AND OTHER FINANCING USES	75,939	(12,367)	88,306	(10,636)	(5,967)	(4,669)
FUND BALANCE July 1, 1995	62,038			163,755		
FUND BALANCE June 30, 1996	$137,977			$153,119		

See accompanying Notes to the Financial Statements.

STATE OF MAINE
PRIMARY GOVERNMENT
COMBINED STATEMENT OF REVENUES, EXPENSES AND CHANGES IN RETAINED EARNINGS AND FUND BALANCES

ALL PROPRIETARY FUND TYPES AND NONEXPENDABLE TRUST FUNDS

For the Year Ended June 30, 1996
(Dollars in Thousands)

	Proprietary Fund Types		Fiduciary Fund Type
	Enterprise	Internal Service	Nonexpendable Trusts
OPERATING REVENUES			
Charges for Services	$225,316	$112,602	$ -
Investment Income	-	-	1,572
Other Operating Revenues	1,061	-	-
TOTAL OPERATING REVENUES	226,377	112,602	1,572
OPERATING EXPENSES			
General Operations	164,876	90,466	-
Depreciation	2,051	5,325	-
Financing Expense-Interest	-	1,011	-
Claims	134	(1,315)	-
Miscellaneous	-	176	-
TOTAL OPERATING EXPENSES	167,061	95,663	-
OPERATING INCOME (loss)	59,316	16,939	1,572
NONOPERATING REVENUES (expenses)	1,120	1,317	-
INCOME (loss) BEFORE OPERATING TRANSFERS	60,436	18,256	1,572
OPERATING TRANSFERS			
Transfers In	2,354	-	-
Transfers Out	(62,516)	-	(549)
TOTAL OPERATING TRANSFERS	(60,162)	-	(549)
NET INCOME	274	18,256	1,023
Add Back Depreciation on Assets Acquired with Contributed Capital	1,865	-	-
INCREASE IN RETAINED EARNINGS	2,139	18,256	1,023
RETAINED EARNINGS (deficits) AT July 1, 1995 AS RESTATED	6,067	21,016	11,333
Equity Transfer	3,447	7,039	-
Balance From General Long-term Obligations Account Group		(63,874)	
RETAINED EARNINGS (deficits) AT June 30, 1996	$11,653	($17,563)	$12,356
CONTRIBUTED CAPITAL AT July 1, 1995	$45,663	$4,941	
Add: Capital Contributions	12,063		
Less: Depreciation of Fixed Assets Acquired with Contributed Capita	(1,865)		
CONTRIBUTED CAPITAL AT June 30, 1996	$55,861	$4,941	

See accompanying Notes to the Financial Statements.

STATE OF MAINE
PRIMARY GOVERNMENT
COMBINED STATEMENT OF CASH FLOWS

ALL PROPRIETARY FUND TYPES AND NONEXPENDABLE TRUST FUNDS

For the Year Ended June 30, 1996
(Dollars in Thousands)

	Proprietary Fund Types		Fiduciary Fund Type
	Enterprise	Internal Service	Nonexpendable Trusts
CASH FLOWS FROM OPERATING ACTIVITIES			
OPERATING INCOME (loss)	$59,316	$16,939	$1,572
Net effect of Increase (decrease) of Equity Transfer	374	(374)	
ADJUSTMENTS TO RECONCILE OPERATING INCOME (loss) TO NET CASH PROVIDED BY OPERATING ACTIVITIES			
Depreciation	2,051	5,325	-
Changes In Assets And Liabilities:			
Investments of Nonexpendable Trust Funds	-	-	(899)
Loans	(360)	374	-
Other Receivables	426	(155)	-
Due from O her Funds	1,063	4,114	-
Inventory	1,031	745	-
Other Assets	(480)	17,676	(5)
Accounts Payable	977	(4,771)	-
Accrued Payroll	(6)	360	-
Compensated Absences	(24)	(44)	-
Due to Other Funds	(1,700)	980	-
Deferred Revenues	(209)	395	-
Claims Payable	(80)	(15,168)	-
Lottery Prizes Payable	837	-	-
Other Accrued Liabilities	(670)	(5,850)	7
TOTAL ADJUSTMENTS TO OPERATING INCOME	3,230	3,607	(897)
NET CASH PROVIDED BY (used for) OPERATING ACTIVITIES	62,546	20,546	675
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES			
Transfers In (out)	(56,715)	7,039	(550)
NET CASH PROVIDED BY (used for) NONCAPITAL FINANCING ACTIVITIES	(56,715)	7,039	(550)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES			
Acquisition and Construc ion of Capital Assets	(13,688)	(16,550)	-
Capital Contributions	12,063	-	-
NET CASH PROVIDED BY (used for) CAPITAL AND RELATED FINANCING ACTIVITIES	(1,625)	(16,550)	-
CASH FLOWS FROM INVESTING ACTIVITIES			
Interest Income	1,120	1,317	-
NET CASH PROVIDED BY (used for) INVESTING ACTIVITIES	1,120	1,317	-
NET INCREASE (decrease) IN CASH AND CASH EQUIVALENTS	5,326	12,352	125
CASH AND CASH EQUIVALENTS July 1, 1995	5,136	10,648	787
CASH AND CASH EQUIVALENTS June 30, 1996	$10,462	$23,000	$912
RECONCILIATION TO COMBINED BALANCE SHEET			
Cash and Cash Equivalents at June 30, 1996	$10,462	$23,000	$912
Cash with Fiscal Agent per the Combined Balance Sheet	-	(671)	-
Cash and Short Term Investments per the Combined Balance Sheet	$10,462	$22,329	$912

NONCASH INVESTING, CAPITAL AND NONCAPITAL FINANCING ACTIVITIES

Beginning of Year Residual Equity Transfer of Accounts Receivable, O her Assets, Deferred Revenue and Claims Payable Between the Internal Service Fund and the Enterprise Fund.		$374	
Transfer of Beginning of Year Liability from the General Long-Term Obligation Account Group		($63,874)	

See accompanying Notes to the Financial Statements.

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State of Maine
Notes to the Financial Statements
June 30, 1996

NOTE 1

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The accompanying financial statements include all funds and the General Long-Term Obligations Account Group of the primary government of the State of Maine (the State). The General Fixed Assets Account Group is not included. The financial statements do not include the financial information of component units of the State of Maine's reporting entity as defined by Governmental Accounting Standards Board (GASB) Statement No. 14 "The Financial Reporting Entity." The GASB is the recognized standard-setting body for establishing governmental accounting and financial reporting principles. The financial statements of the State of Maine have therefore not been prepared in accordance with generally accepted accounting principles (GAAP).

A primary government is a legal entity or body politic and includes all funds, organizations, institutions, agencies, departments and offices that are not legally separate from the State. Component units are legally separate organizations for which the elected officials of the primary government are financially accountable or for which the nature and significance of their relationship with the primary government is such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete. Agencies that appear to meet the criteria for component units include: Maine State Retirement System, Maine Technical College Systems, University of Maine Systems, Maine Maritime Academy, Finance Authority of Maine, Maine State Housing Authority, Maine Educational Loan Authority, Maine Turnpike Authority, Maine Health and Higher Educational Facilities Authority, Loring Development Authority, Maine Court Facilities Authority, and Maine Municipal Bond Bank. The financial information for these entities is not included in the primary government financial statements. Material transactions not in the normal course of business have been disclosed in Note 16, "Related Party Transactions."

Basis of Presentation - Fund Accounting

The State reports its financial position and results of operations in funds and account groups. A fund is a separate accounting entity with a self-balancing set of accounts. Cash and other financial resources, all related liabilities and residual equities, or balances, and changes therein, are recorded and segregated. Each fund's purpose is to carry on specific activities or attain certain objectives in accordance with special regulations, restrictions or limitations. Transactions between funds, if any, have not been eliminated.

Account groups are accounting entities used to provide accountability for the State's general fixed assets and general long-term obligations. They are not considered funds because they do not report expendable available financial resources and related liabilities.

The State has established the following fund categories (further divided by fund types), and account group:

Governmental Funds:
These funds account for the general governmental activities of the State. The General Fund is the primary operating fund of the State. It is used to account for all governmental transactions which are not accounted for in another fund. Special Revenue Funds account for specific revenue sources and the related current liabilities, other than expendable trusts or major capital projects, that are legally restricted to expenditures for specified purposes.

Capital Projects Funds account for financial resources used to acquire or construct major capital assets other than those financed by proprietary funds. These resources are derived primarily from proceeds of general obligation bonds. The State also includes in this fund type proceeds from bond issues for uses other than major capital facilities.

Proprietary Funds:
These funds are used to account for the State's ongoing activities that are similar to those found in the private sector. The activities accounted for in Proprietary Funds include:

Enterprise Funds account for transactions related to resources received and used to finance self-supporting activities of the State. These activities offer products and services on a user-charge basis to the general public.

Internal Service Funds account for transactions related to the financing and sale of goods or services between State agencies. The costs associated with these goods or services are billed to the recipient agency as user charges.

Fiduciary Funds:
These funds are used to account for assets held by the State acting as either a trustee or an agent for individuals, organizations or other funds. The State's fiduciary funds include:

Expendable Trust Funds account for those assets held in a trustee capacity where the principal and income may be expended in the course of the funds' designated operations.

Nonexpendable Trust Funds account for those assets held in a trustee capacity by the State for which only income derived from the trust principal may be expended for designated operations. The principal must be preserved intact.

Agency Funds account for assets the State holds on behalf of others. Agency Funds are custodial in nature and do not involve measurement of operations.

General Long-Term Obligations Account Group:
This account group is used to establish control and accountability for long-term obligations of the State not accounted for in proprietary funds or nonexpendable trust funds. This includes unmatured, long-term obligations related to general obligation bonds, capital leases, Certificates of Participation, compensated absences, and other long-term obligations.

Measurement Focus and Basis of Accounting

Governmental and Expendable Trust Funds are accounted for using a flow of current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized when they become both measurable and available. "Available" means earned and collected or expected to be collected within the current period or soon enough thereafter to be used to pay liabilities of the current period (12 months). Property taxes are recognized as revenue in the year for which they are levied, provided the "available" criterion is met (60 days). Property taxes levied during the current fiscal year for the subsequent period are recorded as deferred revenue during the current year. Property taxes are assessed by the State Tax Assessor on properties located in the Unorganized Territories of Maine and on telecommunications personal properties statewide. Such taxes are levied by April 1; prepayment of one-half of the telecommunications tax is due on June 1 and all other property taxes are due on October 1. Formal collection procedures begin on November 1. Unpaid property taxes become a lien on March 15 of the fiscal year for which they are levied.

Significant revenues susceptible to accrual include income, sales and use, and other taxes, federal grants, federal reimbursements, and other reimbursements for use of materials and services. Revenues from other sources are recognized when received. Expenditures are recorded at the time fund liabilities are incurred. Principal and interest on long-term obligations are recorded as fund liabilities when due.

Proprietary Fund Types and Nonexpendable Trust Funds are accounted for on a flow of economic resources measurement focus and the accrual basis of accounting. With this measurement focus, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. This measurement focus emphasizes the determination of net income. For all proprietary funds, the State applies all applicable Financial Accounting Standards Board (FASB) pronouncements issued on or prior to November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

Agency Fund assets and liabilities are reported using the modified accrual basis of accounting. They are custodial in nature and do not measure results of operations or have a measurement focus.

Cash and Short-Term Investments

The State follows the practice of pooling cash and cash equivalents. Cash equivalents consist of short-term, highly liquid investments that are both readily convertible to known amounts of cash and are near their maturity. The balances pooled are reported at cost which approximates market value. Interest earned on pooled cash is allocated to the various funds based on their average equity balances. Cash with Fiscal Agent in Governmental Funds represents cash that will be used for debt service on bonds. Cash with Fiscal Agent in Proprietary Funds represents proceeds of Certificates of Participation and other financing arrangements that have not been spent.

Short-term investments reported as Cash and Short-Term Investments on the Balance Sheet are comprised primarily of commercial paper, repurchase agreements, US Treasury Bills and Notes.

Investments

Other investments of the State are carried at the lower of cost or market except for investments of the deferred compensation plan which are carried at market value. Donated investments are stated at fair market value at the date of donation.

Unemployment Deposits with United States Treasury

Deposits represent unemployment tax receipts deposited with the United States Treasury. Funds are drawn down as benefits are paid.

Restricted Deposits

Restricted deposits represent funds that have been invested in Certificates of Deposit at various financial institutions within the State. The financial institutions lend these deposits to local commercial and agricultural enterprises to foster economic growth in Maine. Approximately $8.6 million of these funds earn an interest rate 2% below the rate of return otherwise obtainable.

Receivables

Receivables consist primarily of the accrual of taxes; federal revenue and receivables of the State's Medicaid program; amounts due back from service providers for various reasons; and payments required to be made into the unemployment security trust fund. Reimbursements due to the State for its expenditures on federally funded reimbursement and grant programs are included in “Due from Other Governments.” Also included in receivables are amounts due but not yet remitted to the State from lottery sales by agents. Loans receivable represent low interest financing arrangements for the construction and modernization of agricultural storage facilities. Receivables are stated net of estimated allowances for uncollectible amounts, which are determined based upon past collection experience and aging of the accounts (Note 5).

Interfund Transactions

During the course of operations, the State has numerous transactions between funds to finance operations, provide services, and construct assets. To the extent that certain transactions between funds were not completed as of June 30, 1996, interfund receivables or payables have been recorded. Receivables and payables resulting from transactions between funds are classified as “Due from Other Funds” or “Due to Other Funds” on the balance sheet.

Advances to/from other funds are long-term loans made by one fund to another. The advances are offset by a fund balance reserve to indicate they do not constitute expendable financial resources.

Title 28-A, § 64 and Title 8, § 387, of the M.R.S.A. require the Bureau of Alcoholic Beverages and Lottery Operations to transfer all net earnings to the General Fund.

Inventories

The cost of materials and supplies of the governmental funds are reported as expenditures when purchased. Food stamps are stated at coupon value and any unexpended balances at fiscal year end are reported as inventory and deferred revenue in the Special Revenue Fund. Revenues and corresponding expenditures are recognized when the food stamps are issued.

Inventories of materials and supplies in the Proprietary Funds are determined by physical counts and by perpetual inventory systems. Proprietary Fund inventories are stated at cost or average cost, except for the Bureau of Alcoholic Beverages which maintains its inventory on a current replacement cost basis which is not in conformity with GAAP, but approximates FIFO (first in, first out) cost.

Fixed Assets

For Governmental Funds, fixed asset acquisitions are recorded as expenditures in the acquiring fund. Infrastructure assets such as highway curbs, bridges and lighting systems are not capitalized. No interest has been capitalized on self-constructed assets, as noncapitalization of interest does not have a material effect on the financial statements.

Fixed Assets of proprietary funds are accounted for in the acquiring fund. Depreciation is recorded on a straight-line basis over the assets' estimated useful lives which are 2-25 years for equipment and 10-40 years for buildings and improvements.

Tax Refunds Payable

Tax refunds payable primarily represents amounts owed to taxpayers because of overpayments of their 1996 calendar year tax liabilities. Tax refunds payable are accrued to the extent they are measurable based on payments and estimates.

Claims Payable

Claims payable, reported in the proprietary funds of the primary government, represent workers' compensation and other claims payable at June 30, 1996 (Note 12). This includes actual claims submitted, as well as actuarially determined claims incurred but not reported. The liability claims are discounted and presented at their net present value.

Deferred Revenues

Revenues that do not meet the "availability" criterion for recognition in the current period are classified as deferred. Those resources received by the government before it has a legal claim to them are also included as deferred revenues. In subsequent periods, when the revenue recognition criterion is met, or when the government has a legal claim to the resources, the liability for deferred revenue is removed from the balance sheet, and revenue is recognized. The majority of deferred revenues reported in the General Fund is for property tax assessments on telecommunications equipment that does not meet the criteria to be recorded as current year revenue. The majority of deferred revenue in the Federal Expenditures Fund is for food stamps not yet sold.

Due from/to Other Governments

At June 30, 1996, payments were due from the State to various municipalities and school districts. These amounts include general purpose aid for education and the local share of individual income, corporate income, and sales tax revenues (Municipal Revenue Sharing). The amount owed for general purpose aid for education is recorded in the General Fund. The State also owes the federal government for Medicaid cost recoveries from providers. Municipal revenue sharing and Medicaid cost recoveries are recorded in the Special Revenue Fund. Due From Other Governments represents federal grants receivable which is comprised primarily of amounts due for Medicaid claims.

Compensated Absences

Under the terms of union contracts and personnel administrative policies, employees are granted limited amounts of vacation, sick, personal days and compensatory time. Upon separation from state service, employees are eligible for compensation of accrued vacation, personal days, compensatory time and (in some cases) sick leave. For Governmental Funds, vested or accumulated leave expected to be liquidated with current available financial resources is reported as an expenditure and fund liability. Leave that is not expected to be so liquidated is reported in the General Long-Term Obligations Account Group. Compensated absence benefits in the Proprietary Funds are recorded as expenses and liabilities as they accrue.

Other Accrued Liabilities

Other liabilities of the Governmental Funds consist primarily of amounts owed to providers for medical services. The liability for medical services includes an estimate of provider claims for services provided but not billed as of the State's fiscal year end, net of anticipated recoveries. Contractor retainage is included in other liabilities of the Highway Fund.

Long-Term Obligations

The State records long-term debt of governmental funds in the General Long-Term Obligations Account Group. This includes the State's general obligation bonds; governmental fund obligations under capital leases; certificates of participation and other financing arrangements; and long term liabilities for compensated absences. Long-term debt and other obligations financed by proprietary funds, as well as the related interest payments, are recorded as liabilities in the appropriate funds.

Fund Balances

The State reports fund balances as reserved where legally restricted for a specific future use. Otherwise, these balances are considered unreserved. The State has the following reservations:

Reserved for Continuing Appropriations - identifies unexpended amounts in appropriations and encumbrances which the Legislature has specifically authorized to be carried into the next fiscal year.

Reserved for Nonexpendable Trusts - identifies the nonexpendable amount of the trust principal.
Reserved for Unemployment Benefits - identifies amounts reserved for payment of unemployment compensation.

Reserved for Debt Service - identifies amounts held by fiscal agents to fund future debt service obligations.

Reserved for Capital Projects - identifies a legally segregated portion of fund balance available to finance the construction of major capital facilities.

Other Reservations - identifies the amount of fund balance reserved for other specified purposes including working capital needs, long term loans to other funds and contingency funds from which the governor may allocate sums for various purposes.

Total Column-Memorandum Only

The total column on the primary government combined balance sheet is captioned "Memorandum Only" to indicate that it is presented only to facilitate financial analysis. Data in this column does not present a consolidated financial position. Interfund eliminations have not been made in the aggregation of this data.

Future Adoption of Accounting Pronouncements

The GASB has issued the following statements that the State has not yet adopted and which require adoption subsequent to June 30, 1996:

Statement No.	Description	To Be Adopted In Fiscal Year
27	Accounting for Pensions by State and Local Government Employers	1997
28	Accounting and Financial Reporting for Securities Lending Transactions	1997
30	Risk Financing Omnibus-An Amendment of GASB Statement No. 10	1997

The implication of these statements to the State's fiscal practices and financial reports is being evaluated.

Other Accounting Disclosures

During the fiscal year ended June 30, 1996, the State changed its method of accounting for certain taxpayer assessed revenues, including income tax, sales and use tax, fuel tax, and hospital excise tax. The period of availability for the recording of revenue was increased from two months to 12 months in order to recognize tax revenues in the year in which they are earned. The effect of this change on prior periods is reflected in the cumulative effect adjustment on the combined statement of revenues, expenditures and changes in fund balances. The effect of this change is to decrease current year excess of revenues and other financing sources over expenditures and other financing uses by $12 million in the General Fund, and $1.5 million in the Special Revenue Fund.

Prior to fiscal year 1996, expenditures for construction of fixed assets for certain transportation related Enterprise Funds were recorded in the Special Revenue Fund and Capital Projects Fund and transferred to the Enterprise Funds as contributed capital upon completion. Beginning in fiscal year 1996, the expenses of construction are capitalized as Construction in Progress within the Enterprise Funds and transferred to the appropriate fixed asset category upon completion in order to improve accountability for fixed assets in the transportation-related Enterprise Funds. The effect of this change increased the amount of fixed assets and Contributed Capital reported in the Enterprise Funds by $13.5 million. The change has no effect on net income or retained earnings.

In fiscal year 1996, the State reported its debt service activities in the General and Special Revenue Funds rather than in a separate Debt Service Fund.

The State created three new funds in the fiscal year ended June 30, 1996.

1. An Enterprise Fund was created pursuant to 5 M.R.S.A. § 1737, to provide risk management insurance to eligible entities that were not part of the primary government (Note 13). Prior to 1996 these activities were accounted for in one Internal Service Fund. The separation was done to allow the State to more closely match services with the cost of providing those services. The

effect on retained earnings was a decrease in the Internal Service Fund and an increase in the Enterprise Fund of $3.6 million.

2. An Internal Service Fund was created to account for financing activities related to Workers' Compensation, and to establish a more actuarially sound method for accumulating resources to cover related liabilities. General government Workers' Compensation activities were previously reported within the Governmental Funds and General Long-term Obligations Account Group. The effect on the General Long-term Obligations Account Group is a reduction of the liability for Workers' Compensation and a decrease in retained earnings in the Internal Service Funds of $63.9 million.

3. Prior to July 1, 1995, the Maine State Retirement System (MSRS) administered post retirement health care benefits for the State. As of July 1, 1995, Title 5, § 17152 effectively repealed the M.S.R.S.'s administration of the program. It is now accounted for as an Internal Service Fund of the State.

NOTE 2

BUDGETARY PROCESS

In accordance with statute, the Governor presents a proposed budget biennially to the Legislature. The Legislature enacts the budget through a series of specific appropriation and allocation bills for the General Fund and Special Revenue Funds. Effective November 27, 1995, a State constitutional amendment provides the Governor a "line item" veto of dollar amounts, allowing a dollar substitution for those amounts disapproved as long as the appropriation or allocation is not increased either in that line or in any other line in the legislative document. Another constitutional amendment requires the State to fund at least 90 percent of the annual cost of future mandates imposed on local governments, unless overridden by a two-thirds vote of the elected members in both the House and Senate.

Once passed and signed, the budget becomes the financial plan. It sets forth proposed expenditures for all departments and agencies, interest and debt redemption charges, and expenditures for capital projects to be undertaken and executed during each fiscal year. The budget also sets forth the anticipated revenues and any other additional means of financing expenditures proposed for each fiscal year.

Budgetary control is maintained at the account level at which appropriations and allocations are approved by the Legislature, including those pertaining to the required funding of mandates imposed by the State on local municipalities, principally through a quarterly allotment system. Budget revisions during the year, reflecting program changes or intradepartmental administrative transfers, may be effected with Executive and Legislative branch approval. Except in specific instances, only the Legislature may transfer appropriations between departments. In order to provide sufficient funding for several programs during the year ended June 30, 1996, supplemental appropriations of $2.5 million were required.

Encumbrance accounting which requires that purchase orders, contracts and other commitments be recorded to reserve a portion of the appropriation or allocation for expenditure, is employed as an extension of formal budgetary control. Appropriated and allocated balances are available for subsequent expenditure to the extent that encumbrances have been approved by the end of the fiscal year. Since they do not constitute expenditures or liabilities, encumbrances outstanding at year-end are reported as reservations of fund balances representing those portions of fund balances that are not available for allocation or expenditure or that are legally segregated for specific future uses. Unencumbered appropriations in the General Fund and in the Highway Fund lapse at year-end unless, by law, they are carried forward to a subsequent year.

The State's budget is prepared primarily on a cash basis and differs from generally accepted accounting principles (GAAP). A reconciliation of the General Fund and Special Revenue Fund to GAAP basis as presented in the accompanying financial statements is as follows:

Budget to GAAP Reconciliation
June 30, 1996

(Dollars in Thousands)

	General Fund	Special Revenue Funds
Fund Balance, Budgetary Basis	$137,977	$153,119
Perspective Differences:		
Receipts and Other Financing Sources Over (under) Disbursements and Other Financing Uses for Funds Treated as Debt Service in the Financial Plan and Part of the General Fund for GAAP Reporting	2,842	-
Basis of Accounting Differences:		
Due (to) from Federal Government	(29,129)	203,284
Taxes Receivable (payable)	89,686	16,093
Tax Refunds	(55,200)	-
Deferred Revenues	(41,795)	-
Due (to) from Other Funds	743	161
Accrued Revenues (expenditures)	(65,374)	(218,957)
Fund Reclassification	10	-
Fund Balance, GAAP Basis	$39,760	$153,700

<u>NOTE 3</u>

DEFICIT FUND BALANCES/RETAINED EARNINGS

Two Internal Service Funds have fund deficits at June 30, 1996. There was a deficit of $927,000 in the Retained Earnings of the Telecommunications fund and a deficit of $46.2 million in the Workers' Compensation fund. The deficit in the Workers' Compensation fund reflects the accrual of the actuarial liability of $50.2 million. The Telecommunications deficit is being reduced by an increase in rates charged.

NOTE 4

DEPOSITS AND INVESTMENTS

The deposit and investment policies of the State of Maine Office of the Treasurer are governed by Title 5 of the Maine Revised Statutes Annotated. Per § 135, the Treasurer of State may deposit State funds, including trust funds of the State, in any of the banking institutions; trust companies; State or federal savings and loan associations; or mutual savings banks organized under the laws of this State or in any national bank or federal savings and loan associations located in the State. When there is excess money in the State Treasury which is not needed to meet current obligations, the Treasurer of State may invest those funds in certain investments, with the concurrence of the State Controller or the Commissioner of Administrative and Financial Services and with the consent of the Governor. Approved investments include bonds; notes; certificates of indebtedness; other obligations of the United States that mature not more than 24 months from the date of investment; repurchase agreements secured by obligations of the United States that mature within the succeeding 24 months; prime commercial paper; tax-exempt obligations; or bankers' acceptances. State funds may also be deposited as required by the terms of custodial contracts or agreements negotiated in accordance with the laws of this State.

Investment policies of the permanent trust funds are governed by Title 5, § 138. According to this statute, the Treasurer of State, with the approval of the Commissioner of Administrative and Financial Services, the Superintendent of Banking, and the Commissioner of Education, may invest the funds in such securities that are legal investments in accordance with Title 9-B. The investment policies of the Percival P. Baxter expendable trusts, as stated in the late Governor's last will and testament, provide only that the funds may be managed, invested, reinvested and administered within the trustee's discretion.

The State Treasurer may also participate in the securities loan market by lending State owned bonds, notes or other certificates of indebtedness of the federal government if they are fully collateralized by treasury bills or cash. In addition, the State Treasurer may invest up to $4 million in lending institutions at a 2% lower-than-market yield, provided the financial institutions lend operating funds (at least equal to the amount of the deposit) to agricultural enterprises in this State at 2% interest rate reductions. The Treasurer may also invest up to $4 million in lending institutions at a 2% lower-than-market yield, provided the financial institutions lend operating funds (at least equal to the amount of the deposits) to commercial enterprises approved by the Treasurer at 2% interest rate deductions.

No amounts exceeding 25% of the capital, surplus, and undivided profits of any trust company or national bank or 25% of the reserve fund and undivided profits of a mutual savings bank or State or federal savings and loan association shall be on deposit therein at any one time. The restriction does not apply to deposits subject to immediate withdrawal to meet the payment of any bonded debts, or interest, or to pay current bills or expenses of the State. Also exempt are those deposits secured by the pledge of certain securities as collateral, and deposits fully covered by insurance. The collateral shall be in an amount equal to the deposit. The value of the securities pledged shall be determined by the Treasurer of State on the basis of market value.

Deposits

Deposits with financial institutions are classified as to collateral risk into the following three categories. Category 1 is the amount of State deposits that are fully insured or collateralized with securities held by the State or its agent in the State's name. Category 2 is the amount of deposits that are collateralized with securities held by the pledging financial institutions' trust departments or agents in the State's name. Category 3 is the amount of deposits that are not collateralized or insured.

Deposits by Category (All Funds)
June 30, 1996

(Dollars in Thousands)

	1	2	3	Bank Balance	Carrying Amount
Cash and Short-Term Investments	$20,694	$ -	$10,155	$30,849	($9,073)
Cash with Fiscal Agent	-	-	27,002	27,002	27,002
Restricted Deposits	-	-	10,606	10,606	10,606
Total	$20,694	$ -	$47,763	$68,457	$28,535

Investments

Investments are also classified to indicate the level of risk assumed by the State. Category 1 consists of investments that are insured or registered or for which the securities are held by the State or its agent in the State's name. Category 2 is those investments that are uninsured and unregistered, with securities held by the counterparty's trust department or agent in the State's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty, or by its trust department or agent but not in the State's name.

Investments by Category (All Funds)
June 30, 1996

(Dollars in Thousands)

	1	2	3	Carrying Amount	Market Value
Short-Term Investments:					
Repurchase Agreements	$ -	$137,019	$ -	$137,019	$137,156
U.S. Treasury Bills	-	83,920	-	83,920	85,010
Commercial Paper	-	105,588	-	105,588	106,015
	-	326,527	-	326,527	328,181
Investments:					
U.S. Treasury Bills	-	4,476	7,933	12,409	12,317
Commercial Paper	-	6,970	20,303	27,273	34,643
	$ -	$11 446	$28 236	39,682	$46 960
Investments of Deferred Compensation Plan				111,443	
Assets Held in Trust				38,265	
Total				$515,917	

Following is a reconciliation of the balance of cash and short term investments at June 30, 1996:

Reconciliation of Cash and Short Term Investments
June 30, 1996

(Dollars in Thousands)

Carrying amount of Cash and Short-Term Investments	($9,073)
Carrying Amount of Short -Term Investments	326,527
Cash and Short-Term Investments	$317,454

NOTE 5

RECEIVABLES

Taxes, federal reimbursements, loans and other receivables are presented in the various funds as follows:

Detail of Amounts Receivable
June 30, 1996

(Dollars in Thousands)

	Taxes	Due from Federal Government	Loans	Other	Allowance for Uncollectibles	Net Receivable
General Fund	$312,935	$ -	$ -	$35,519	($124,243)	$224,211
Special Revenue Funds	62,848	109,694	1,468	39,716	(5,859)	207,867
Trust and Agency	-	-	-	4,620	(2,488)	2,132
Internal Service Funds	-	-	-	499	-	499
Enterprise Funds	-	-	9,873	10,089	(222)	19,740
Subtotal	375,783	109,694	11,341	90,443	($132,812)	454,449
Less: Allowance for Uncollectibles	126,238	-	-	6,574		-
Net Receivables	$249,545	$109,694	$11,341	$83,869		$454,449

NOTE 6

INTERFUND TRANSACTIONS

Due to/from Other Funds

Due to Other Funds are amounts owed by one State fund to another for goods sold or services rendered. Due from Other Funds are amounts to be received from one State fund by another for goods sold or services rendered. The following is a summary of due from other funds, and due to other funds at June 30, 1996:

Schedule of Due to/from Other Funds
June 30, 1996

(Dollars in Thousands)

Fund Type	Due From	Due To
General:	$2,949	$11,621
Special Revenue:		
Highway	26	2,312
Other Special Revenue	8,677	2,845
Total Special Revenue	8,703	5,157
Enterprise:		
Alcoholic Beverages	-	54
State Lottery	1	1,528
Other Enterprise	12	21
Total Enterprise	13	1,603
Internal Service:		
Telecommunications	1,934	1,608
Risk Management	1,088	3
Data Processing	2,103	11
Other Internal Service	3,354	154
Total Internal Service	8,479	1,776
Trust and Agency:	13	-
Total All Funds	$20,157	$20,157

During August 1995, the Telecommunications Internal Service Fund accounts payable balance of $7 million at June 30, 1995 was reduced by approximately $4 million. The reduction was the result of approximately $500,000 in credits negotiated with the service provider and a loan of $3.5 million from the State's General Fund. The loan from the General Fund was authorized by Public Law 1995, Chapter 368 § U-1. Chapter 368 requires that payment (at an interest rate of 5%) be made from the Telecommunications Fund, no later than February 1, 1997. At June 30, 1996, the amount the Telecommunication Fund owed the General Fund was $1.5 million and is included in the schedule above.

Advances to/from Other Funds

Advances from the General Fund are for inventory of the Bureau of Alcoholic Beverages (an Enterprise Fund), and various projects of the Departments of Economic & Community Development and Environmental Protection (Special Revenue Funds). Advances from the Highway Fund (a Special Revenue Fund) represents a working capital advance to Motor Transport Service (an Internal Service Fund) for the purchase of equipment, land and buildings. The following is a summary of interfund advances at June 30, 1996:

Schedule of Advances to/from Other Funds
June 30, 1996

(Dollars in Thousands)

	Advances	
Fund Type	Receivable	Payable
General	$2,086	$ -
Special Revenue	13,217	1,000
Proprietary:		
Alcoholic Beverages	-	1,000
Motor Transport Service	-	13,303
Total All Funds	$15,303	$15,303

NOTE 7

FIXED ASSETS

The following schedule details fixed assets that are recorded in funds other than the General Fixed Assets Account Group:

Summary of Fixed Assets in Proprietary Funds
June 30, 1996

(Dollars in Thousands)

	Enterprise Funds	Internal Service Funds
Land	$850	$251
Buildings	3,840	5,106
Equipment	55,686	108,406
Improvements Other Than Buildings	345	220
Construction in progress	13,466	-
Less: Accumulated Depreciation	(20,590)	(65,777)
Total Fixed Assets	$53 597	$48 206

NOTE 8

MAINE STATE RETIREMENT SYSTEM (Unaudited)

The following selected financial information was reported in separately issued, audited financial statements. The Maine State Retirement System has been audited by Coopers & Lybrand L.L.P., for the year ended June 30, 1996, and that report is available from the Maine State Retirement System, 2 Central Plaza, Augusta, ME 04330. The information presented below includes all activity of the Retirement System. Required information separately presented for the State is not available.

Plan Description

The Maine State Retirement System (System) is a body corporate and politic and an incorporated public instrumentality of the State. It is the administrator of an agent multiple-employer defined benefit public employee retirement system established and administered under Title 5 M.R.S.A., C. 421, 423 and 425. The System provides pension, death and disability benefits to its members. Members include employees of the State; public school employees who are defined by Maine law as teachers and for whom the State pays the employer retirement contributions; and employees of approximately 250 local municipalities and other public entities in Maine, each of which contracts for participation in the System under provisions of the relevant statutes. The System acts as the common investment agent for the State and all other participating entities. At June 30, 1996, the approximate membership consisted of:

Active vested and non-vested members	47,494
Inactive members	51,366
Retirees and beneficiaries	27,031
Other benefit recipients	1,989
Total members, retirees and beneficiaries	127,880

The System's retirement programs provide defined retirement benefits based on members' average final compensation and creditable service. Vesting occurs upon the earlier of ten years' service credit or the earning of one year's service credit immediately preceding retirement at or after normal retirement age. Normal retirement age is 60 or 62, determined by whether a member had at least 10 years of creditable service on June 30, 1993. The monthly benefit is reduced by a statutory prescribed factor for each year that a member is below the normal retirement age. The System also provides death and disability benefits, which are established by statute for State and public school employees, and by contract with other participating employers under applicable statutory provisions.

Upon termination of membership, members' accumulated employee contributions are refundable with interest, credited for a five year period for non-vested members and through the date of refund for vested members. Withdrawal of accumulated contributions results in forfeiture of all benefits. The annual rate of interest credited to members' accounts is set by the System's Board of Trustees and is currently 6.5%.

In the event that a participating entity withdraws from the System, its individual employee-members can terminate membership or remain contributing members. The participating entity remains liable for contributions sufficient to fund benefits for its already retired former employee-members, for its terminated vested inactive members, and for those active employees, whether or not vested, who remain contributing System members.

Retirement benefits are funded by contributions from members and employers as well as earnings from investments. Disability and death benefits are funded by employer contributions and investment earnings. Member and employer contributions are a percentage of applicable member compensation. Member contribution rates are defined by law and depend on the terms of the plan under which a member is covered. Employer contribution rates are determined by annual actuarial valuations.

The System also provides group life insurance under a plan that is administered by a third party insurance company. Premiums are set and collected by the System. Benefit payments are made by the insurance company from premiums collected. Any shortfall of benefit payments over premiums collected is remitted by the System to the insurance company.

Funding Status and Progress

The amount shown below as "pension benefit obligation" is a standardized disclosure measure of the present value of pension benefits, adjusted for the effects of projected salary increases, estimated to be payable in the future as a result of employee service to date. The measure is the actuarial present value of credited projected benefits and is intended to help users assess the System's funding status on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among public employee retirement plans. The measure is independent of the actuarial funding method used to determine contributions to the System.

The pension benefit obligation was determined as part of actuarial valuations at June 30, 1996, and 1995. Significant actuarial assumptions used include: a) a rate of return on the investment of assets of 8% per year compounded annually, b) projected cost of living increases for eligible benefit recipients of 4% per year compounded annually, attributable to inflation, and c) projected salary increases of 6% to 10% per year attributable to seniority/merit and inflation.

At June 30, 1996, the unfunded pension benefit obligation was:

Unfunded Pension Obligation
June 30, 1996

(Dollars in Millions)

Pension Benefit Obligation:	
Retirees and Beneficiaries Currently Receiving Benefits and Terminated Employees Not Yet Receiving Benefits	$ 3,037.7
Current Employees:	
Accumulated Employee Contributions, Including Allocated Investment Income	1,123.4
Employer-financed Vested	1,200.5
Employer-financed Non-vested	1,360.5
Total Pension Benefit Obligation	6,722.1
Net Assets Available for Benefits, at Cost	3,065.1
Unfunded Pension Benefit Obligation	$ 3,657.0

In addition, the System's Group Life Plan has unfunded benefit obligations of approximately $77 million, which consists of the present value of benefit obligations of $104 million, offset by net assets available for benefits of $27 million. The present value of the benefit obligation was calculated with an assumed discount rate of 8%.

Contributions Required and Made

The System's funding policy provides for periodic employer contributions at actuarially determined rates. Expressed as percentages of annual covered payroll, these rates are sufficient to accumulate adequate assets to pay benefits when due. Level percentages of payroll employer contribution rates are determined using the entry age normal actuarial funding method. The System also uses the level percentage of payroll method to amortize the unfunded liability of the State and teacher plan(s) over a closed 35 year period.

Plan members are required by statute to contribute 7.65% of earnable compensation or have "pickup" contributions made at a rate of 7.65% of earnable compensation. "Pickup" contributions are defined by statute as member contributions which are assumed and paid by the employer through a reduction of members' salaries for services rendered in lieu of employee contributions. The contribution rate differs for special groups of State employees.

Contributions totaling $356.8 million ($253.7 million employer and $103.1 million employee), were made in accordance with actuarially determined contribution requirements established through an actuarial valuation performed at June 30, 1996.

Significant actuarial assumptions used to compute contribution requirements are the same as those used to compute the standardized measure of the pension obligation.

Trend Information

Historical trend information gives an indication of the progress made in accumulating sufficient assets to pay benefits when due. For 10 year historical supplementary information, see separately issued MSRS financial statements. The standardized measure of the pension obligation is available beginning with fiscal year 1995. The following schedule is a two-year analysis of the funding progress of the System.

Funding Progress of the Maine State Retirement System
June 30, 1996

(Dollars in Thousands)

	Net Assets Available for Benefits	Pension and Group Life Benefit Obligation	Percentage Funded	Unfunded Pension and Group Life Benefit Obligation	(Unaudited) Annual Covered Payroll	(Unaudited) Unfunded Pension and Group Life Benefit Obligation as a Percentage of Covered Payroll
1996	$ 3,092,090	$ 6,826,148	45.3%	$3,734,057	$1,316,462	283.6
1995	2,750,522	5,687,258	48.4%	2,936,736	(A)	(A)

(A) Information regarding annual covered payroll is not available.

Employer contributions in dollars and as a percentage of annual covered payroll follow. These contributions were all made in accordance with actuarially determined and statutory requirements.

Maine State Retirement System Contributions
June 30, 1996

(Dollars in Thousands)

	Member Contributions	State and Local Agency Contributions	(Unaudited) Member, State and Local Agency Contributions as a Percentage of Annual Covered Payroll	Net Investment Income	Total Revenues
1996	$ 103,117	$ 253,647	27.1%	$ 291,724	$ 648,488
1995	106,727	244,106	(A)	164,582	515,415

(A) Information regarding annual covered payroll is not available.

In November 1995, voters in the State approved a constitutional amendment that requires the State to fund the unfunded liabilities which existed as of June 30, 1996, in the State and teacher plan(s). The funding must commence by June 30, 1997, over a period not to exceed 31 years. The creation of new unfunded liabilities is prohibited, except those arising from experience losses. Such liabilities must be funded over a period of not more than ten years. In addition, the amendment requires use of actuarially sound current cost accounting, reinforcing the existing statutory requirements.

NOTE 9

OTHER POSTEMPLOYMENT EMPLOYEE BENEFITS

Post Retirement Health Care Benefits

In addition to providing pension benefits, the State of Maine funds health care benefits for most retirees. Public Laws of 1995, Chapter 368 § G-3 and G-4 repealed the provision that required payment by the Maine State Retirement System for retirees' health insurance premiums. The State subsequently assumed administrative responsibility for post retirement health care insurance premium payments.

Any employee who is eligible for group health insurance pursuant to 5 M.R.S.A. § 285 is eligible for retiree health benefits, including: most state employees and legislators, and employees of the Maine Turnpike Authority, the Maine Technical College System, the Maine Maritime Academy and the Maine State Retirement System. Specifically excluded (5 M.R.S.A. § 285 1-B) are members of the Maine Municipal Association and the Maine Teachers Association, and employees of counties and municipalities and their instrumentalities. Benefits for teachers are addressed in 20-A M.R.S.A. §13451 et seq.; the State pays 25 % of post retirement health insurance premiums for teachers. The State pays 100% of post retirement health insurance premiums for other eligible individuals who were first employed before July 1, 1991. A pro rata portion, ranging from 0% for retirees with less than 5 years participation to 100% for retirees with 10 or more years of participation, is paid for eligible individuals first employed after July 1, 1991. Retirees eligible for Medicare are covered under supplemental insurance policies. Coverage for retirees who are not eligible for Medicare includes basic hospitalization, supplemental major medical and prescription drugs, and costs for treatment of mental health, alcoholism and substance abuse.

Funds for post retirement health care benefits are transferred on a weekly basis to an Internal Service Fund account. Expenditures are recognized by the State as premiums are paid, using funds generated by current employer contributions. For the fiscal year ended June 30, 1996, there were 6,787 retired eligible State and Technical College employees and 7,737 retired teachers.

The State does not segregate payments to insurers by funding source. In 1996, the State expended $16.3 million for premium payments, including direct payments by the Maine State Retirement System. The amount provided by participants cannot be determined: generally, the portion of premium charges that are not paid by the State for retired teachers is borne by the individual teachers. A balance of $4.9 million remained in the newly-created retiree health Internal Service Fund.

Retiree health care benefits are funded on a pay-as-you-go basis. During the fiscal year ended June 30, 1996, funds were provided by the following sources:

Health Insurance Premiums Paid into the
Retiree Health Insurance Fund
June 30, 1996

(Dollars in Thousands)

	Teachers	State Employees	Technical College Employees
Maine State Retirement System (funds remaining)	$ 2,500	$ 7,900	$ -
Employer Contribution*	-	9,300	800
Legislative Appropriation	657	-	-
	$3,157	$17,200	$800

* A rate of 3.8%, reduced to .53% for State employees, and a rate of 3.8% for Technical College System employees, were applied to current payroll.

Postretirement Life Insurance Benefits

In addition to providing pension and health care benefits and in accordance with statutory authority the State of Maine through the Maine State Retirement System (MSRS) provides certain life insurance benefits for retired employees who, as active employees, participated in the Group Life Insurance Program for a minimum of 10 years. Payments of claims are made by MSRS from a fund containing a percentage of the monthly State paid basic life insurance premiums of active State employees, basic life insurance premiums of active teachers and earnings on the investments of the fund. In addition to the cost of claims, the State pays a monthly retention fee to a life insurance company. Retired State employee and retired teacher life insurance claims totaled $2.8 million for the fiscal year ended June 30, 1996. The number of participants eligible to receive benefits at fiscal year ended 1996 cannot be readily determined.

Other Postemployment Benefits

Upon termination from active employment with the State, individuals may qualify for continuation of health and dental benefits, for an 18 month period after date of termination. This coverage is mandated by and complies with the Consolidated Omnibus Budget Reconciliation Act (COBRA). Individuals participating under COBRA will be responsible for the entire monthly premium, plus an additional 2% to cover administrative costs. There were 100 former employees covered under COBRA at June 30, 1996.

NOTE 10

DEFERRED COMPENSATION

The State offers its employees a deferred compensation plan created in accordance with Internal Revenue Code § 457. The plan, available to all State employees, permits them to defer a portion of their salary until future years. The deferred compensation is not available to employees until the employee retires, resigns, or otherwise leaves State employment; becomes disabled, and his claim is approved by the Advisory Council; or suffers an unforeseen financial emergency.

All amounts of compensation deferred under the plan, all property and rights purchased with those amounts, and all income attributable to those amounts, property, or rights are (until paid or made available to the employee or other beneficiary) solely the property and rights of the State (without being restricted to the provisions of benefits under the plan), subject only to the claims of the State's general creditors. Participants' rights under the plan are equal to those of the general creditors of the State in an amount equal to the fair market value of the deferred account for each participant.

The financial liability of the State is limited in each instance to the payment of premiums and the purchase of shares under the deferred compensation program while the enrolled remains an employee of the State, and only to the amount of the compensation or portion of compensation held for payment of such premiums or shares. In the past, the plan assets have been used only to pay benefits. The State believes that it is unlikely that it will use the assets to satisfy the claims of general creditors in the future.

NOTE 11

LONG-TERM OBLIGATIONS

The State records its liability for bonds in the General Long-Term Obligations Account Group. Other general long-term obligations recognized by the State are its obligations under Certificates of Participation and other financing arrangements, obligations under capital leases, compensated absences, and claims and judgments. Payments for these liabilities will be made from the governmental funds. Prior to fiscal year 1996, the State had included obligations for workers' compensation in the General Long-term Obligations Account Group. These are now accounted for in an Internal Service Fund.

During the year ended June 30, 1996, the following changes occurred in liabilities reported in the General Long-Term Obligations Account Group:

General Long-Term Obligations
June 30, 1996

(Dollars in Thousands)

	Bonds	Certificates of Participation and Other Financing Arrangements	Capital Leases	Compensated Absences	Workers' Compensation	Total
Balance, July 1, 1995	$516,060	$9,870	$19,040	$32,077	$63,874	$640,921
Issuances	76,700		848	-	-	77,548
Payments	77,070	1,825	969	-	-	79,864
Other Increase (decrease)	-	-	-	(5,965)	(63,874)	(69,839)
Balance, June 30, 1996	$515,690	$8,045	$18,919	$26,112	$ -	$568,766

General Obligation Bonds

State of Maine bonds are issued pursuant to sections 14, 14-A, 14-B, 14-C, and 14-D of Article 9 of the Maine State Constitution. Bonds issued pursuant to section 14 have been authorized by two-thirds of the House and Senate and by the citizens of Maine through bond referendums. They are general obligation bonds, backed by the full faith and credit of the State. These bonds are retired through the use of State appropriations and are repaid in annual installments beginning not more than one year after issuance. Debt service principal and interest payments for General Fund and Highway Fund bonds are appropriated and paid from the General Fund and Highway Fund, respectively.

Self-liquidating bonds are general obligation bonds issued for quasi-state agencies. Transfers from the Maine Veterans' Home, State colleges and vocational institutions are made for the required debt service.

During fiscal year 1996, the State issued bonds in the amount of $76.7 million for removal of oil storage tanks, clean up of hazardous substance sites, construction of water pollution control facilities, capping of solid waste landfills, construction and renovation of correctional facilities, improvements to airport, cargo port and ferry service facilities, training equipment for the Maine Technical College System, housing for people with special needs, and statewide telecommunications equipment.

The following schedule presents the changes in general obligation bonds of the State of Maine:

Changes in General Obligation Bonds
June 30, 1996

(Dollars in Thousands)

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	Balance July 1, 1995	Retirements	Additions	Balance June 30, 1996
General Fund	$377,055	$59,297	$51,700	$369,458
Highway Fund	136,950	17,510	25,000	144,440
Self-liquidating	2,055	263	-	1,792
	$516,060	$77,070	$76,700	$515,690

The future debt service requirements for the bonds are as follows:

Future Debt Service on General Obligation Bonds
June 30, 1996

(Dollars in Thousands)

Fiscal Year	Principal	Interest	Total
1997	$88,180	$27,214	$115,394
1998	71,305	22,689	93,994
1999	65,735	18,985	84,720
2000	59,705	15,545	75,250
2001	57,445	12,218	69,663
Thereafter	173,320	22,219	195,539
Total	$515,690	$118,870	$634,560

Any bonds not issued within five years of the date of ratification may not be issued after that date. Within two years after expiration of the five year period, the Legislature may extend, by a majority vote, the five year period for an additional five years or may deauthorize the bonds. If the Legislature fails to take action within those two years, the bond issue shall be considered to be deauthorized and no further bonds may be issued.

A summary of general obligation bonds authorized by voters and unissued at June 30, 1996, follows:

General Obligation Bonds Authorized and Unissued
June 30, 1996

(Dollars in Thousands)

Purpose	Unissued July 1, 1995	New Authorizations	Deauthorizations	New Sales	Unissued June 30, 1996
Environment and Conservation	$23,000	$14,000	$1,250	$21,500	$14,250
Corrections	2,500	-	-	2,500	-
Education	4,301	15,000	1	6,700	1,600
Highway Improvements	1,500	58,900	-	39,500	20,900
Other Purposes	5,500	4,000	-	6,500	14,000
Totals	$36 801	$91 900	$1 251	$76 700	$50 750

Bond and Tax Anticipation Notes

In July 1995, the State issued $182 million of general obligation tax anticipation notes (TANs) at 4.5% with a maturity date of June 28, 1996. General obligation tax anticipation notes are authorized by Article 9 Section 14 of the Maine State Constitution. The July 1995 TANs were issued to improve the State's cash position.

During fiscal year 1996, bond anticipation notes (BANs) totaling $26.8 million were issued by the State with interest rates ranging from 3.7% to 4.1% and a maturity date of May 15, 1996. The BANs were issued as a temporary financing vehicle for new projects that were ultimately financed with bond issuance proceeds. The BANs are backed by the full faith and credit of the State. As of June 30, 1996, there are no BANs outstanding.

Certificates of Participation and Other Financing Arrangements

Certificates of Participation - Governmental Funds

Since 1988, the State has entered into various financing arrangements for the construction of certain State buildings through the issuance of Certificates of Participation. These certificates are issued through a trustee and the State is responsible for payments to the trustee that approximate the interest and principal payments made to the certificate holders. The State maintains custody and use of the buildings, however, the trustee holds a lien as security until such time as the certificates are fully paid. The Certificates of Participation do not constitute a debt or liability within the meaning of any constitutional or statutory limitation, or a contractual obligation in excess of the amounts appropriated therefor, and the State has no continuing legal or moral obligation to appropriate money for future minimum payments or other obligations under any agreement. Each agency's obligation to make its minimum payments or any other obligation under its agreement are subject to and dependent upon appropriations being made by the Legislature of the State.

Future Debt Service on Certificates of Participation
June 30, 1996

(Dollars in Thousands)

Year Ending June 30,	Minimum Payments
1997	$ 2,302
1998	1,901
1999	1,803
2000	1,703
2001	1,601
Thereafter	-
Total Minimum Payments	$ 9,310
Less: Amount Representing Interest	1,265
Present Value of Future Minimum Payments	$ 8,045

Certificates of Participation and Other Financing Arrangements - Proprietary Funds

The State has entered into various financing arrangements, through its Internal Service Funds, for the purchase of equipment through the issuance of Certificates of Participation and other financing arrangements. The liability for payment of these obligations and the related assets are recorded directly in the fund from which payment will be made.

Future Debt Service on Certificates of Participation and Other Financing Arrangements for Proprietary Funds
June 30, 1996

(Dollars in Thousands)

	Minimum Payments	
Year Ending June 30,	Certificates of Participation	Other Financing Arrangements
1997	$7,896	$ 608
1998	7,128	581
1999	4,389	555
2000	4,167	-
2001	-	-
Total Minimum Payments	23,580	1,744
Less: Amount Representing Interest	2,280	159
Present Value of Future Minimum Payments	$21,300	$1,585

Obligations Under Capital Leases

The State does not maintain adequate systems to identify, classify and report capital leases in conformity with generally accepted accounting principles. As such, it is not possible to present the amount of assets recorded under such leases, their accumulated amortization or disclose the future minimum lease payments at net present value.

NOTE 12

SELF-INSURANCE

Risk Management

The State maintains several types of self-insurance plans. These include property, vehicle, boat and aircraft, tort, civil rights, employee bonds, police professional, and workers' compensation.

The plan allocates the cost of providing claims servicing and claims payment by charging a "premium" to each agency based on a review of past losses and estimated losses for the current period. All risk financing liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Claims liabilities are actuarially determined based on estimates of the ultimate cost of claims, including future claim adjustment expenses, that have been incurred but not reported and claims reported but not settled. Claims liabilities are reevaluated periodically to take into consideration recently settled claims, the frequency of claims, and other economic and social factors. Because actual claims liabilities depend on such complex factors as inflation, changes in legal doctrines, and damage awards, the process used in computing claims liability does not necessarily result in an exact amount.

Commercial insurance has been purchased for losses that exceed the following limits: buildings, $1 million; boat hulls, $100,000; aircraft, $50,000; and boat liability, $10,000. Aircraft liability is insured from the first dollar. There is a fund depletion policy that contributes money to the fund when the year's claims exceed $2.5 million in the aggregate for police professionals, vehicles, civil rights, and tort.

Annuity contracts have been purchased for the purpose of settling certain claims. Information is insufficient to determine the amount of the claims liabilities outstanding for which annuity contracts have been purchased in the claimant's name, and the amount of the related liabilities which have been removed from the balance sheet.

At June 30, 1996, $2.41 million was reported as the estimated claims payable for the State's self-insurance plan. The discounted amount is $2.18 million and was calculated based on a 6% yield on investments. There have not been any significant reductions in insurance since last year.

Changes in the balance of claims and judgments liabilities during fiscal 1996 were:

Risk Management Fund Claims Payable
June 30, 1996

(Dollars in Thousands)

		Amount
Liability at Beginning of Year		$1,727 *
Current Year Claims and Changes in Estimates		1,554
Claims Payments		(1,102)
Liability at End of Year	(discounted)	$2,179

* Prior to Fiscal Year 1996, the Risk Management Internal Service Fund and the Public Entity Risk Pool Enterprise Fund (Note 13) were reported as one fund. As a result, liability information for the prior year is not available for the individual funds. The Internal Service Fund's pro-rated liability (not discounted) is $1.7 million as of the beginning of the year.

Unemployment Insurance

The State is self-insured for unemployment compensation. As a direct reimbursement employer for all unemployment compensation the State recognizes all costs for unemployment compensation as claims are paid. These costs totaled $1.64 million for the fiscal year ended June 30, 1996.

Workers' Compensation

Workers' compensation is accounted for in an Internal Service Fund. Interfund premiums are treated as quasi-external transactions. Each State agency is charged a "premium" based on the number of employees to be covered plus an added amount to reduce the unfunded liability. The Legislature, Legislative Council and Law Library employees are self-insured for workers' compensation purposes. The State assumes the full risk of all claims filed for workers' compensation.

Until June 30, 1995, the Workers' Compensation Division initially made claims payments on a pay as you go basis and was then reimbursed for the payment amount by the individual State department whose employee was injured and filed the claim. The claims liability was recorded in the General Long-Term Obligations Account Group. It was organized as an internal service fund on July 1, 1995. The Workers' Compensation Internal Service Fund assumed all liability for outstanding losses that previously were paid by individual departments. Annuity contracts have been purchased for the purpose of settling certain claims. Information is insufficient to determine the amount of the claims liabilities for which annuity contracts have been purchased in the claimant's name, and the amount of the related liabilities which have been removed from the balance sheet.

Based on actuarial calculations, as of June 30, 1996, the State is liable for unfunded claims and incurred but not reported claims. The claims total approximately $68.9 million. The discounted amount is $50.2 million and was calculated based on a 6% yield on investments.

Changes in the balance of claims and judgments liabilities during fiscal 1996 were as follows:

Workers' Compensation Liability
June 30, 1996

(Dollars in Thousands)

	Amount
Liability at Beginning of Year	$63,874*
Current Year Claims and Changes in Estimates	(1,318)
Claims Payments	(12,356)
Liability at End of Year	$50,200

* Prior to Fiscal Year 1996, the Workers' Compensation liability was disclosed in the notes to the financial statements at its face value, although discounted figures were recorded in the General Long-term Obligations Account Group. As a result, prior year information is not comparable and not presented.

Health Care

The State of Maine's health insurance plan provides insurance coverage for active employees of the state as well as several quasi-governmental agencies. The State is insured under a retrospectively rated insurance policy from a commercial insurer as a group plan with the Maine Technical College System, the Maine Turnpike Authority and other smaller quasi- governmental entities.

Rates were set to generate working premiums totaling $98.3 million of which the State group represented approximately 88%. If actual loss experience for the period required less then $98.3 million of working premiums, then a credit would be due from the carrier. If loss experience for the period required more then $98.3 million of working premiums then the participant groups would be liable for an additional 10% or $9.8 million. The insurance carrier is responsible for loss experience beyond $108.1 million.

At June 30, 1996, the contract cycle with the health care insurer had ended. At the termination of that cycle, a final cost settlement is to be determined. The final settlement had not been concluded as of the report date and therefore any receivable or payable that may result had not been determined but is not believed to be material.

Disability

State law allows confidential employees who become temporarily disabled to receive 66.67% of their salary for up to 335 calendar days. There were approximately 853 confidential employees at June 30, 1996. The expenditure amount for this benefit cannot be determined.

NOTE 13

PUBLIC ENTITY RISK POOL

The State provides risk management insurance advice and services to public instrumentalities other than State departments or agencies. If there is a strong public need; coverage is otherwise unavailable; or is offered only at unreasonable cost to that person or entity; and if the Governor has approved that person or entity for insurance services, they are eligible for such services. These instrumentalities are primarily educational entities such as The University of Maine System, the Maine Technical College System, and the Maine Maritime Academy. During the fiscal year ended June 30, 1996, approximately 50 individual persons or entities participated in this pool.

The risk pool is accounted for in an Enterprise Fund. Prior to FY 1996, this fund was combined with the self-insurance fund for State agencies (Note 12). The fund was split by allocating the unused contributions to the respective funds. The risk pool participates on an equal basis in the commercial insurance and fund depletion policy described in the Internal Service Fund. Statute provides that persons or entities participating in the State-administered fund do not have a right of recovery except against the assets of the State-administered fund and do not have recourse against any State assets or State employees. It also provides that the assets of the fund may not be transferred to meet a budgetary shortfall or pay uninsured expenses.

Claims liabilities are actuarially determined based on estimates of the ultimate cost of claims, including future claim adjustment expenses, that have been incurred but not reported and claims reported but not settled. Because actual claims liabilities depend on such complex factors as inflation, changes in legal doctrines, and damage awards, the process used in computing claims liability does not necessarily result in an exact amount. A provision for inflation in the calculation of estimated future claims costs is implicit in the calculation. Reliance is placed both on actual historical data that reflects past inflation and on other factors that are considered to be appropriate modifiers of past experience. Anticipated investment income is considered in setting rates for the fund. Annuity contracts have been purchased for the purpose of settling certain claims. Information is insufficient to determine the amount of the claims liabilities for which annuity contracts have been purchased in the claimants' name, and the amount of the related liabilities which have been removed from the balance sheet.

Based on actuarial calculations, as of June 30, 1996, $336,000 is reported as the estimated claims payable for the State administered risk pool. The discounted amount is $306,000 and was calculated based on a 6% yield on investments. The estimated losses are based upon actual claims that have been submitted as well as claims incurred but not reported. The following schedule shows the changes in the reported liability since June 30, 1995.

Public Entity Risk Pool Claims Payable
June 30, 1996

(Dollars in Thousands)

	Amount
Unpaid Claims and Claims Adjustment Expenses at Beginning of Fiscal Year	$546
Incurred Claims and Claims Adjustment Expenses:	
Provision for Insured Events of the Current Fiscal Year	64
Increases in Provision for Insured Events of Prior Fiscal Years	40
Total Incurred Claims and Adjustment Expenses	104
Payments:	
Claims and Claims Adjustment Expenses Attributable Insured Events of the Current Fiscal Year	165
Claims and Claims Adjustment Expenses Attributable to Insured Events of the Prior Fiscal Year	179
Total Payments	$344
Total Unpaid Claims and Claims Adjustment Expenses at End of Fiscal Year (discounted)	$306

* Prior to Fiscal Year 1996, the Risk Management Internal Service Fund (Note 12) and the Public Entity Risk Pool Enterprise Fund were reported as one fund. As a result, liability information for the prior year is not available for the individual funds. The Enterprise Fund's pro-rated liability (not discounted) is $546,000 as of the beginning of the year.

NOTE 14

SEGMENT INFORMATION

The State has the following Enterprise Funds which have been created to provide various services to the general public:

Enterprise Fund Selected Information
June 30, 1996

(Dollars in Thousands)

	Lottery Operations	Bureau of Alcoholic Beverages	Risk Pool	D.O.T Related	Agriculture Related	Other Enterprise Funds	Total Enterprise Funds
Operating Revenues	$150,323	$71,558	$1,082	$2,257	$407	$750	$226,377
Depreciation Expense	20	90	-	1,865	60	16	2,051
Operating Income (loss)	38,991	23,325	397	(2,410)	(559)	(428)	59,316
Net Nonoperating Revenues	400	-	221	44	433	22	1,120
Net Income (loss)	23	241	554	(287)	151	(408)	274
Operating Transfers in (out)	(39,368)	(23,084)	(64)	2,077	277	-	(60,162)
Additions to (from) Property, Plant and Equipment	(27)	24	-	(13,652)	(25)	(9)	(13,689)
Total Assets	10,490	6,802	4,317	53,122	12,208	794	87,733
Total Long-Term Liabilities	-	1,000	-	-	1,731	-	2,731
Total Liabilities	10,490	6,802	316	638	1,841	132	20,219
Total Equity	-	-	4,001	52,485	10,367	662	67,515
Net Working Capital	(52)	696	4,001	100	1,522	508	6,775
Current Capital Contributions (reductions)	-	(524)	-	12,586	-	-	12,062

NOTE 15

JOINT VENTURES

Joint ventures are independently constituted entities generally created by two or more governments for a specific purpose. The only material joint venture in which the State participates is the Tri-State Lotto Commission.

The Tri-State Lotto Commission (Commission) was established in 1985 pursuant to passage into law of the Tri-State Lotto Compact by the States of Maine, New Hampshire and Vermont. The Commission is authorized and empowered to promulgate rules and regulations regarding the conduct of lottery games, including the price or prices of tickets, the number and size of prizes for winning tickets, and the licensing of agents.

The Commission is composed of one member from each of the participating states. Each compact member state lottery or sweepstakes commission appoints one of its members to serve on the Commission. Each member shall hold office at the pleasure of the appointing authority. The Commissioner shall elect a chairman from among its members, annually.

The Commission has designated that 50% of its operating revenue be aggregated in a common prize pool. A prize award liability is established when the winning ticket number is selected. If no winning ticket is selected, the available jackpot is carried over to the following drawing. The Tri-State Lotto Compact requires that prizes not claimed within one year from the date of the drawing are forfeited. All unclaimed prizes are credited to future prize pools. The Commission funds its jackpots through annuity contracts purchased from insurance companies and zero-coupon US Government Treasury Strips.

A proportional share of revenue and expenses are allocated to each State based on the amount of ticket sales made by each State. Exceptions are the facility's management fee, which is based on a contracted percentage of operating revenue that varies from state to state; Daily Number expenses that are allocated to each State based on Daily Number ticket sales; and certain other miscellaneous costs that are based on actual charges generated by each state.

The financial statements of the Tri-State Lotto Commission may be obtained at the Bureau of Alcoholic Beverages and Lottery Operations, 8 State House Station, Augusta, ME 04333.

As of and for the year ended June 29, 1996, the following selected financial information was reported in the audited financial statements of the Tri-State Lotto Commission:

Tri-State Lotto Commission
June 30, 1996

(Dollars in Thousands)

Current Assets	$ 41,637
Non-Current Assets	216,515
Total Assets	$ 258,152
Current Liabilities	$ 37,426
Long-Term Liabilities	215,731
Total Liabilities	253,157
Retained Earnings (designated prize reserves)	4,995
Total Liabilities and Retained Earnings	$ 258,152
Total Revenue	$ 104,480
Total Expenses	$ 68,126
Allocation of Funds to Member States	$ 36,354
Increase in Retained Earnings	$ -

NOTE 16

RELATED PARTY TRANSACTIONS

The State of Maine provides funding to some of the entities that are deemed component units of the primary government (Note 1). These entities include the Maine Technical College System, the University of Maine System, Maine Maritime Academy, Finance Authority of Maine, Maine School of Science and Mathematics and Maine Science and Technology Foundation. Appropriations for these organizations for the year ended June 30, 1996, totaled $180.9 million. Other information pertaining to these organizations that would be required in conformity with FASB No. 57, "Related Party Disclosures," has not been included.

In 1995, the Finance Authority of Maine provided financing in the amount of $2 million to the State of Maine, Department of Agriculture, Food and Rural Resources. The balance of this note payable at June 30, 1996, is $1.7 million. These funds were specifically earmarked for the Potato Marketing Improvement Fund, which provides direct, fixed rate loans to growers and packers for the construction and retrofitting of modern potato storage and packing facilities, and the acquisition and installation of packing equipment. This is a seven year note with principal and interest due through 2001 in annual installments of $340,000. The note bears an interest rate of 5% for the first year and is adjusted annually thereafter based on the one year US Treasury Bill yield. This note is secured by the assets of the Potato Marketing Improvement Fund, which primarily consist of financial assets such as short term investments and notes receivable.

On July 1, 1996, the Maine Turnpike Authority (the Authority), a component unit of the State of Maine, issued $35.3 million in special obligation bonds as authorized by PL 1995, C 504 §C-5, which carry interest rates of 4.25% to 5% and mature from July 1, 1997 through July 1, 2006. Bond proceeds were to be conveyed to the Maine Department of Transportation (MDOT) and were to be used to pay a portion of highway or bridge project costs. The bonds are payable solely from special obligation revenues of the Authority. The bonds do not constitute a pledge of full faith and credit of the State of Maine or a debt of the State of Maine or any agency of the State. The annual transfer of operating surplus from the Authority to the MDOT will be reduced by the debt service requirements of the bonds.

The Maine Court Facilities Authority has issued bonds for the purpose of financing the acquisition and construction of court facilities for use by the Judicial Department of the State of Maine. The State of Maine entered into lease agreements with the Authority. These agreements call for the State to make lease payments sufficient to pay the debt service of the Authority. The State's obligation to make lease payments and any other obligations under the lease agreements are subject to and dependent upon appropriations being made by the State Legislature for such purposes.

The Maine Department of Transportation (MDOT) is responsible for management of the Motor Transport Services (MTS) Internal Service Fund. MTS derives 92% of its revenues from the rental of heavy equipment to MDOT. In the 1996 fiscal year, MTS refunded $2 million to MDOT because equipment rental charges were higher than anticipated. As of June 30, 1996, MDOT owed approximately $348,000 to MTS for current billings and MTS owed the MDOT $13.2 million for working capital advances made between 1947 and 1987.

NOTE 17

COMMITMENTS AND CONTINGENCIES

Federal Grants

The State receives significant financial assistance from the federal government. The receipt of grants is generally dependent upon compliance with terms and conditions of the grant agreements and applicable federal regulations, including the expenditure of resources for allowable purposes. Grants are subject to the Federal Single Audit Act. Disallowances by federal officials as a result of these audits may become liabilities of the State. The amount of expenditures which may be disallowed by the grantor agencies cannot be determined at this time.

Municipal Solid Waste Landfills

Title 38 MRSA § 1310-F establishes within the Department of Environmental Protection a cost sharing program for the closure and remediation of solid waste landfills which pose an actual or potential hazard to the environment and public health. The State's obligation to provide cost sharing to municipalities is subject to the availability of general obligation bond funds approved for that purpose. At June 30, 1996, $59 million had been authorized and issued for solid waste landfill closure and remediation with $56 million expended or encumbered. At June 30, 1996, the estimated cost of future landfill closure and remediation projects is not known. In the 1996 fiscal year $13 million in bond funds was expended for solid waste landfill projects.

Construction Commitments

At June 30, 1996, the Department of Environmental Protection had contractual commitments for pollution abatement construction projects as provided for by Title 13 MRSA § 411. Subject to approval by the Commissioner, the State may contribute to the design, engineering and construction of municipal pollution abatement facilities. At June 30, 1996, $100 million in general obligation bond funds had been authorized for pollution abatement construction projects, $90 million had been issued and $85 million expended. The amount of bond funds committed in contracts to these projects at June 30, 1996 was $5 million. The estimated cost of future pollution abatement construction projects is not known. In the 1996 fiscal year, $10 million in bond funds was expended on pollution abatement projects.

A portion of the payment that is made to municipalities for General Purpose Aid to Local Schools is allocated for debt service. This portion represents the subsidy for debt service resulting from local outstanding indebtedness for school construction and renovation projects. As of June 30, 1996, outstanding commitments by municipalities for school construction projects totaled $674.7 million.

At June 30, 1996, the Department of Transportation had contractual commitments of approximately $103.4 million for construction of various highway projects. The State's share of that amount is expected to be approximately $21.6 million. Funding for these future expenditures is expected to be provided from federal funds, State funds, and bond proceeds.

Contingent Receivable

At June 30, 1996, the Maine Department of Transportation (MDOT) had unreimbursed expenditures paid from the Highway Fund in fiscal years 1996 and prior. Based on historical experience, these expenditures are potentially reimbursable, in part, by the federal highway program through project modifications. The MDOT has not determined the probability or estimated the amount of any reimbursement.

Constitutional Obligations

Article 9, § 14-A, of the Maine State Constitution provides that the State may insure the payment of mortgage loans on real estate and personal property within the State for industrial, manufacturing, fishing, agricultural and recreational enterprises. The aggregate of these obligations may not exceed $90 million at any one time. As of June 30, 1996, amounts committed pursuant to this authorization were $61.5 million.

Article 9, § 14-C, of the Maine State Constitution provides that the State may insure the payment of mortgage loans for the acquisition, construction, repair and remodeling of houses owned or to be owned by members of two tribes on several Indian reservations. These loans may not exceed $1 million in the aggregate at any one time. As of June 30, 1996, amounts committed pursuant to this authorization were approximately $84,000.

Article 9, § 14-D, of the Maine State Constitution provides that the State may insure the payment of any mortgage loan to resident Maine veterans of the Armed Forces of the United States, including loans to a business organization owned in whole or in part by a resident Maine veteran. These loans may not exceed $4 million in the aggregate at any one time. As of June 30, 1996, amounts committed pursuant to this authorization were $1.4 million.

Article 8, § 2, of the Maine State Constitution provides that the State may secure funds for loans to Maine students attending institutions of higher education. Funds shall be obtained by the issuance of State bonds, when authorized by the Governor. The amount of bonds issued and outstanding shall not at any one time exceed $4 million in the aggregate. As of June 30, 1996, there were no amounts issued pursuant to these authorizations.

Moral Obligations

Statutes governing certain public Authorities provide for Capital Reserve Provisions. These provisions authorize the State to make up any deficiencies in their debt service reserve funds, subject to legislative appropriation, effectively constituting a moral obligation to back the Authorities' credit. Since such moral obligations do not constitute full faith and credit obligations of the State, voter approval of such obligations is not required. The State has never been called upon to make any direct payments pursuant to such provisions. As of June 30, 1996, approximately $2.6 billion in moral obligation bonds were outstanding and the required debt service reserve was $258.4 million.

Issuing Authorities, bonds outstanding, required debt reserve, moral obligation debt limits and the legal citation for each Authority appear in a table on the following page.

Moral Obligation Bonds
June 30, 1996

(Dollars in Thousands)

Issuer	Bonds Outstanding	Required Debt Reserve	Moral Obligation Debt Limit	Legal Citation
*Finance Authority of Maine	$ 242,278	$37,771	$ 591,000	10 MRSA §1032, 1053
Maine Educational Loan Authority	31,360	2,386	50,000	20-A MRSA §11424
Maine Municipal Bond Bank	841,430	99,030	No Limit	30-A MRSA § 6006
Maine Health and Higher Educational Facilities Authority	556,410	43,623	No Limit	22 MRSA § 2075
Loring Development Authority	0	0	100,000	5 MRSA §13080-N
Maine State Housing Authority	998,000	75,622	1,150,000	30-A MRSA § 4906
Total	$2,669,478	$258,432		

* It is the opinion of the State's legal counsel that statutory history provides substantial support for the conclusion that the legislature intended that these bonds be secured by the moral obligation of the State.

NOTE 18

LITIGATION

The State of Maine, its units and employees are parties to numerous legal proceedings, many of which normally occur in governmental operations. In the opinion of the Attorney General and other legal counsel representing the State, it is not probable that the legal proceedings will have a material adverse impact on the State's financial position. Therefore, the State has not recorded liabilities in anticipation of awarded or anticipated unfavorable judgments.

In all the cases listed below, except in the case of the Consent Decrees, the Attorney General advises that the State, its agencies and employees have valid defenses and that the State is vigorously defending the claims. The State is also a party to various legal proceedings, which, if resolved in the State's favor, would result in contingency gains to the State's General Fund balance, without material effect upon fund balance. The ultimate dispositions and consequences of all these proceedings are not presently determinable, but it is not probable that the ultimate disposition of any single proceeding or all legal proceedings collectively will have, in the opinion of the State's Attorney General and the Department of Administrative and Financial Services, any material adverse effect on the State's financial position.

The State is a defendant in two class actions lawsuits, Bates v. Peet, et al., and Consumer Advisory Board, et al. v. Glover, et al., which were settled by Consent Decrees applicable to the mental health and mental retardation services provided by the Department of Mental Health, Mental Retardation, and Substance Abuse Services. In both cases, the State remains subject to the terms of the Decrees and believes that it can meet the requirements within its existing budget, but it is possible that additional funds could be required as a result of future court orders.

The State is a defendant in SC Testing Technologies v. Maine, DEP et al., a contract case seeking damages of $42 million arising out of the State's repeal of legislation requiring that automobiles be tested prior to registration. The State prevailed in both the Maine Superior and Supreme Judicial Courts. Plaintiff recently filed a petition for certiorari to the United States Supreme Court on only one of the original multiple grounds for suit - the claim that the State is federally preempted from amending Maine laws on auto emission testing by the terms of the federal Clean Air Act. It is believed that there is only a remote chance that the US Supreme Court will agree to that review.

Parker v. Wakelin and Dzialo v. Perrier are two lawsuits seeking judgments that certain legislative changes made to save money in the State Retirement System are unconstitutional. The Parker case involves teachers who work for local school districts but who are members of the Maine State Retirement System. In that case the State lost on certain significant issues before the United States District Court for the District of Maine, and an appeal is pending. However, the Attorney General believes that Maine's appeal raises significant issues on which the State has a reasonable chance of prevailing. The Dzialo suit, which involves similar legislative changes as they impact directly on State employees, was filed in December of 1996. It is likely that the outcome of the Parker case will be largely dispositive of the Dzialo case. If the Parker decision below is not reversed on appeal, it has been estimated that the Legislature will be required to increase the annual funding for the Retirement Plan (for both teachers and State employees) by an amount that has been estimated at $16 million for FY 1998 and larger amounts in future years. Plaintiffs have cross appealed on those issues on which the State prevailed at the District Court level, and if Plaintiffs prevail on their appeal, the annual cost to the State (for both teachers and State employees) has been estimated at an additional $22 million for FY 1998, a figure that will also increase over time.

The State is also a defendant in an administrative reimbursement action brought by the federal Department of Health and Human Services arising out of a dispute concerning the proper allocation of pension contribution costs between the State and federal government. The case, which arose out of a federal audit for fiscal year 1991-92, is currently pending before the federal Department of Health and Human Services Departmental Appeals Board. The claim in dispute is approximately $7 million, although the State has asserted setoffs nearly equaling the amount claimed by DHHS.

The federal government has not pursued an unasserted claim in an amount ranging from $5.7 to $7.7 million in the Medicaid Program. The claim arises out of a State of Maine Gross Receipts Tax in effect from July 1993 to December 1993 that the federal government claims was inappropriate. The law was amended effective December 1993, and later repealed. This is a national issue which affects many states and it is possible that federal legislation may resolve the matter prior to any potential administrative reimbursement action.

The State is in receipt of a Notice of Claim demanding $7 million for damages based on the death of a patient at the Augusta Mental Health Institute. This claim includes both a claim against the State under the Maine Tort Claims Act and claims against state employees and contractors under state and federal law. No lawsuit has been filed. Even if liability were found, it is not probable that the damages would approach the amount claimed.

State employees are defendants or potential defendants in several civil rights actions in which large dollar amounts have been claimed. The State cannot itself be sued under the applicable civil rights laws but could be responsible for certain defense costs in such suits and also self-insures certain of its employees up to a maximum of $300,000 for any one occurrence.

The State of Maine has been audited by the IRS and the IRS has taken the position that the State owes employment taxes on independent contractors that the IRS alleges qualify as employees under federal tax law and owes limited FICA payments. This dispute is currently pending before the IRS at the administrative level. After an initial assessment of over a million dollars, after completion of the audit phase, the IRS has reduced the assessment to less than $450,000 for the tax year 1993. The State is filing an administrative appeal.

The State is a defendant in a number of tort claims actions. These cases, whether at the notice of tort claim stage or filed as court actions, are subject to the limitations stated in the Maine Tort Claims Act, 14 M.R.S.A §8101 et seq., of $300,000 per occurrence, a bar on punitive or exemplary damages, and complete immunity for an array of discretionary actions. It is not probable that the State's aggregate exposure will exceed $10 million.

The State is a party to numerous other legal proceedings, such as tax reimbursement actions, many of which recur in government operations. As noted above, the State is defending the actions. In the opinion of the Attorney General, even if liability is found in some of these cases, it is not probable the damages awarded will have any material effect on the financial condition of the government.

NOTE 19

FUND BALANCE RESTATEMENT

General Fund fund balance at June 30, 1995, as reported in the Primary Government Combined Statement of Revenues, Expenditures and Changes in Fund Balances, has been decreased by $59.8 million to reflect the proper accrual of Tax Refunds Payable during fiscal year 1995.

NOTE 20

SUBSEQUENT EVENTS

Bond Authorizations

Subsequent to June 30, 1996, voters approved bond issues of $40.5 million and $4.9 million. The proceeds are to fund major improvements at state parks and historic sites, encourage and support economic development, construct water pollution control facilities, address environmental health deficiencies in drinking water supplies, investigate abate and clean up hazardous substance discharges, clean up tire stockpiles, close and clean up municipal solid waste landfills, and connect libraries and communities electronically.

Tax Anticipation Notes

On July 2, 1996, the State issued $150 million of general obligation tax anticipation notes with an interest rate of 4.5% and a maturity date of June 27, 1997. These notes were issued to provide cash flow to the General Fund during fiscal year 1997.

Bond Anticipation Notes

Subsequent to fiscal year 1996, bond anticipation notes (BANs) totaling $10.125 million were issued by the State with interest rates ranging from 4% to 4.15% and maturities in May and June, 1997. The BANs were issued as a temporary financing vehicle for new projects that will be financed with future bond proceeds.

Lease /Financing Arrangements

The State entered into a lease financing agreement with the Maine Court Facilities Authority for the financing of court facilities in Skowhegan and Biddeford. The total principal amount financed is $5.9 million, the amortization of which will begin September 1, 1997. The State entered into three other financing agreements subsequent to fiscal year end. The total principal amount financed is $4.3 million. The financing was for computer equipment and motor vehicles, and is administered within the Internal Service Fund.

Repeal of Gross Receipts Tax

Effective January 1, 1997, legislation repealed the seven percent gross receipts tax charged to consumers for nursing home care. For fiscal year 1996, these taxes resulted in approximately $25 million.

Individual Income Tax Ceiling Repealed

Chapter 24 Public Laws of 1997 repealed 36 MRSA § 5111-B, which had become effective June 1995. The repealed statute had mandated individual income tax rate reductions and tax refunds once a certain targeted revenue amount was reached. The statute had never been applied, as the targeted amount had not been reached.

Revised Hospital Financing Plan

In the spring of 1997 the State of Maine, in cooperation with Maine hospitals and following discussions with the federal government, developed a revised plan for payments to and from hospitals. The purpose of the plan was to phase out the "tax and match" financing arrangement by June 30, 1998, with the minimum possible disruption. The plan results in an increase in the hospitals' tax burden in the 1997 and 1998 years with a compensating increase in the state's commitment to the hospitals to pay for bad debt and charity cases (the disproportionate share program). The increase in the disproportionate share reimbursement rate was applied retroactively to July 1, 1995. The retroactive provision resulted in additional accruals in the accompanying financial statements of $14 million in expenditures, $22 million in accounts payable, $8 million in accounts receivable, and $9.3 million due from the federal government. Because these amounts involve the Medicaid program, 36% is reflected in the General Fund and 64% in the Federal Expenditures (Special Revenue) Fund.

Lease of Augusta State Airport

As of December 1, 1996, the State of Maine, through the Department of Transportation, has entered into a lease/purchase agreement with the City of Augusta for the City to operate, and eventually own, the facilities of the Augusta State Airport, currently accounted for as an Enterprise Fund.

The lease terms also provide for the Department of Transportation to pay an annual subsidy to the City of Augusta for airport purposes, and for the City to remit income from airport operations to the Department.

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Independent Auditor's Report on Supplementary Schedule of Federal Financial Assistance

To the President of the Senate and the
Speaker of the House of Representatives

We have audited the primary government financial statements of the State of Maine, as of and for the year ended June 30, 1996, and have issued our qualified report thereon dated March 31, 1997. These primary government financial statements are the responsibility of the State of Maine's management. Our responsibility is to express an opinion on these primary government financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards; *Government Auditing Standards*, issued by the Comptroller General of the United States; and the provisions of Office of Management and Budget (OMB) Circular A-128, *Audits of State and Local Governments*. Those standards and OMB Circular A-128 require that we plan and perform the audit to obtain reasonable assurance about whether the primary government financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the primary government financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 2C, the accompanying schedule is prepared primarily on the cash basis of accounting. Consequently, certain expenditures are recognized when paid rather than when the obligation is incurred.

State of Maine
Schedule of Federal Financial Assistance
For the Year Ended June 30, 1996

Schedule A

Recipient/Grantor Agency	Federal Catalog Number	Program Title	Expenditures 1996
		Major Federal Programs	
			$
Department of Economic and Community Development			
U.S. Department of Housing and Urban Develop.	14.228	Community Development Block Grants /State's Program	17,909,895
		Total Department of Economic and Community Development	**17,909,895**
Department of Education			
U.S. Department of Agriculture	10.555	National School Lunch Program	15,910,872
U.S. Department of Education	84.010	Title I Grants - LEA'S	25,067,890
	84.027	Special Education - State Grants	12,925,053
	84.048	Vocational Education - Basic Grants to States	4,752,889
	84.126	Rehabilitation Services - Voc. Rehab. Grants to States	12,139,076
		Total Department of Education	**70,795,780**
Department of Human Services			
U.S. Department of Agriculture	10.551	Food Stamps (Note 3B)	112,764,561
	10.557	Special Supplemental Food Prog. - Women, Infants, Children	12,277,934
	10.558	Child and Adult Care Food Program	11,503,849
	10.561	State Admin. Matching Grants for Food Stamp Program	6,294,240
U.S. Department of Health and Human Services	93.560	Family Support Payments to States - Assistance Payments	61,222,836
	93.561	Job Opportunities and Basic Skills Training	6,260,057
	93.563	Child Support Enforcement	9,244,361
	93.658	Foster Care - Title IV-E	17,235,161
	93.667	Social Services Block Grant	13,034,006
	93.778	Medical Assistance Program	629,263,671
	93.802	Social Security - Disability Insurance	4,770,363
		Total Department of Human Services	**883,871,039**
Department of Labor			
U.S. Department of Labor	17.207	Employment Service	4,557,296
	17.225	Unemployment Insurance (Note 3F)	19,909,395
	17.246	Employment & Training Assistance - Dislocated Workers	7,828,047
	17.250	Job Training Partnership Act	8,463,301
		Total Department of Labor	**40,758,039**
Department of Transportation			
U.S. Department of Transportation	20.205	Highway Planning and Construction	143,465,866
		Total Department of Transportation	**143,465,866**
Executive Department - Substance Abuse			
U.S. Department of Health and Human Services	93.959	Blk Gts for Prevent. & Treat. of Substance Abuse	4,271,693
		Total Executive Department - Substance Abuse	**4,271,693**
Total Federal Assistance - Major Programs:		$	**1,161,072,312**

State of Maine
Schedule of Federal Financial Assistance
For the Year Ended June 30, 1996

Schedule A (Continued)

Recipient/Grantor Agency	Federal Catalog Number	Program Title	Expenditures 1996
		Non-Major Federal Programs	**$**
Department of Administrative and Financial Services			
U.S. Department of Transportation	20.205	Highway Planning and Construction	52,177
General Services Administration	39.003	Donated Federal Surplus Personal Property (Note 3E)	218,052
		Total Department of Administrative and Financial Services	**270,229**
Department of Agriculture			
U.S. Department of Agriculture	10.025	Plant and Animal Disease, Pest Control, and Animal Care	40,434
	10.162	Inspection Grading and Standardization	538,579
	10.569	Temp. Emergency Food Assistance - Commodities (Note 3D)	139,369
	10.571	Food Commodities for Soup Kitchens (Note 3D)	521,245
U.S. Environmental Protection Agency	66.461	Wetlands Protection - State and Tribal Development Grants	5,486
	66.700	Cons. Pesticide Compliance Monitoring and Prog. Coop. Agts	249,802
U.S. Department of the Army, Corps of Engineers	OFA	Aroostook Water/Soil Improvement Fund	139,540
U.S. Food & Drug Administration	OFA	Food Inspection Program - Branding Law	2,290
	OFA	Federal & State Inspection Program	976
		Total Department of Agriculture	**1,637,721**
Maine Arts Commission			
National Foundation on the Arts and the Humanities	45.001	Promotion of the Arts - Design Arts	148
	45.002	Promotion of the Arts - Dance	16,243
	45.003	Promotion of the Arts - Arts in Education	81,263
	45.007	Promotion of the Arts - State and Regional Program	502,094
	45.010	Promotion of the Arts - Expansion Arts	40,000
	45.015	Promotion of the Arts - Folk and Traditional Arts	43,960
	45.023	Promotion of the Arts - Local Arts Agencies Programs	60,183
		Total Maine Arts Commission	**743,891**
Atlantic Sea Run Salmon Commission			
National Oceanic & Atmospheric Administration	11.472	Unallied Science Program	169,048
U.S. Department of the Interior	15.600	Anadromous Fish Conservation	211,574
		Total Atlantic Sea Run Salmon Commission	**380,622**
Department of Attorney General			
U.S. Department of Health and Human Services	93.775	State Medicaid Fraud Control Units	350,750
		Total Department of Attorney General	**350,750**
Department of Conservation			
U.S. Department of Agriculture	10.025	Plant and Animal Disease, Pest Control, and Animal Care	4,533
	10.063	Agricultural Conservation Program	1,255
	10.652	Forestry Research	72,159
	10.664	Cooperative Forestry Assistance	984,452
U.S. Department of the Interior	15.612	Rare and Endangered Species Conservation	33,000
	15.808	Geological Survey - Research and Data Acquisition	30,017
	15.916	Outdoor Recreation - Acquisition, Development, & Planning	223,164
U.S. Department of Transportation	20.219	National Recreational Trails Fund Program	27,732
National Science Foundation	47.050	Geosciences	13,793
Small Business Administration	59.045	Forest Management Division	22,958
U.S. Environmental Protection Agency	66.416	Water Pollution Control	21,263

State of Maine
Schedule of Federal Financial Assistance
For the Year Ended June 30, 1996

Schedule A (Continued)

Recipient/Grantor Agency	Federal Catalog Number	Program Title	Expenditures 1996
		Non-Major Federal Programs	**$**
Department of Conservation - continued			
National Biological Service	OFA	Grant Funds for Hollis Training Site	32,758
U.S. Department of Defense	OFA	Agreement for Pre and Post Monitoring Services - Hollis Site	27,928
		Total Department of Conservation	**1,495,012**
Department of Corrections			
U.S. Department of Justice	16.540	Juvenile Justice & Delinquency Prevention - Alloc to States	503,469
	16.603	Corrections - Technical Assistance/Clearinghouse	51,654
U.S. Department of Education	84.255	Literacy Program for Prisoners	27,813
		Total Department of Corrections	**582,936**
Department of Defense and Veterans Services			
U.S. Department of Transportation	20.703	Materials Emergency Preparedness Trng. & Planning Grants	26,186
U.S. Department of Veterans Affairs	64.101	Burial Expenses Allowance for Veterans	45,583
	64.203	State Cemetery Grants	141,137
Federal Emergency Management Agency	83.011	Hazardous Materials Training Program	23,337
	83.503	Civil Defense - Emergency Management Assistance	773,337
	83.505	State Disaster Preparedness Grants	32,255
	83.516	Disaster Assistance	1,571,242
	83.520	Hurricane Program	76,471
	83.528	Emergency Management Institute - Field Training Program	66,605
	83.531	State and Local Emergency Management Assistance - Other	241,232
		Total Department of Defense and Veterans Services	**2,997,385**
Department of Economic and Community Development			
U.S. Department of Commerce	11.307	Special Econ. Develop. and Adj. Assistance Program	1,176,893
U.S. Department of Defense	12.607	Community Economic Adjustment Planning Assistance	108,336
U.S. Department of Energy	81.052	Energy Conservation for Institutional Buildings	195,445
		Total Department of Economic and Community Development	**1,480,674**
Department of Education			
U.S. Department of Agriculture	10.550	Food Distribution Program (Note 3A)	3,074,392
	10.553	School Breakfast Program	2,897,921
	10.556	Special Milk Program for Children	125,446
	10.559	Summer Food Service Program for Children	727,705
	10.560	State Administrative Expenses for Child Nutrition	298,554
	10.564	Nutrition Education and Training Program	70,765
U.S. Department of Education	84.002	Adult Education - State Grant Program	1,239,651
	84.004	Desegregation Assist., Civil Rights Training, and Adv. Svcs.	141,797
	84.009	Education of Handicapped Children in State Schools	4,521
	84.011	Migrant Education - Basic State Grant Program	3,729,140
	84.012	Educationally Deprived Children - State Admin.	191,373
	84.013	Title I Program for Neglected and Delinquent Children	43,137
	84.029	Special Ed. Personnel Development and Parent Training	132,660
	84.049	Vocational Education - Consumer and Homemaker Education	22,112
	84.086	Special Education - Program for Severely Disabled Children	441,010
	84.151	Chapter II - State Block Grants	132,390
	84.158	Sec. Educ. and Transitional Svcs. for Youth w/ Disabilities	266,980

State of Maine
Schedule of Federal Financial Assistance
For the Year Ended June 30, 1996

Schedule A
(Continued)

Recipient/Grantor Agency	Federal Catalog Number	Program Title	Expenditures 1996
		Non-Major Federal Programs	**$**
Department of Education - continued			
	84.161	Rehabilitation Services - Client Assistance Program	86,800
	84.162	Immigrant Education	19,253
	84.164	Eisenhower Mathematics and Science Education - State Gts.	44,058
	84.168	Eisenhower Professional Development - National Activities	426,887
	84.169	Independent Living - State Grants	329,285
	84.173	Special Education - Preschool Grants	2,235,614
	84.177	Rehabilitation Services - Indep Living for Older Blind Indiv	160,431
	84.181	Special Education - Grants for Infants and Families w/ Dis.	2,152,291
	84.185	Byrd Honors Scholarships	129,000
	84.186	Safe and Drug-Free Schools and Comm. - State Grants	1,483,539
	84.187	Supported Employ. Svcs. for Indiv. w/ Severe Disabilities	271,246
	84.190	Christa McAuliff Fellowships	25,598
	84.192	Adult Education - Literacy Training for Homeless Adults	100,767
	84.194	Bilingual Education Support Services	95,839
	84.196	Education of Homeless Children and Youth - State/Local	64,317
	84.199	Vocational Education Cooperative Demonstration	390,000
	84.207	Drug-Free Schools and Comm - School Personnel Training	204,081
	84.213	Even Start - State Educ. Agencies	443,931
	84.216	Private School	10,980
	84.218	State School Improvement Grants	256,758
	84.224	State Grants for Assistive Technology	1,001,791
	84.243	Tech-Prep Education	570,398
	84.249	Foreign Language Assistance	59,255
	84.255	Literacy Program for Prisoners	481,101
	84.265	Rehab. Training - State Voc. Rehab. In-Service Training	15,803
	84.267	State Postsecondary Review	7,739
	84.276	Goals 2000 Educate America Act	832,132
	84.278	Career Opportunities 2000 - Statewide School to Work Sys.	3,388,486
	84.281	Eisenhower Professional Development State Grants	1,252,211
	84.298	Title VI - Innovative Education Program Strategies	1,610,167
U.S. Department of Health and Human Services	93.938	Coop. Agree. School Health Education - HIV/AIDS	304,977
Corporation for National and Community Service	94.004	Learn and Serve America - School and Comm. Based Prog.	108,603
U.S. Department of Education	OFA	School Finance and Enrollment	5,500
U.S. Department of Health and Human Services	OFA	Veterans Education	77,726
		Total Department of Education	**32,186,118**
Department of Environmental Protection			
U.S. Department of Defense	12.113	St. Memo. of Agree. for Reimb. of Technical Services	597,924
U.S. Environmental Protection Agency	66.001	Air Pollution Control - Program Support	1,374,906
	66.419	Water Pollution Control - State/Interstate Program Support	870,921
	66.420	Water Poll. Control - State & Local Manpower Prog. Dev.	35,388
	66.433	State Underground Water Source Protection	60,282
	66.435	Water Poll. Control - Lake Restoration Coop. Agreements	9,889
	66.438	Construction Management Assistance	307,002
	66.454	Water Quality Management Planning	106,605
	66.460	Nonpoint Source Implementation Grants	926,749
	66.461	Wetlands Protection - State and Tribal Development Grants	8,202

Recipient/Grantor Agency	Federal Catalog Number	Program Title	Expenditures 1996
		Non-Major Federal Programs	**$**
Department of Environmental Protection - continued			
	66.463	Nat'l Pollutant Disch. Elimination System Rel. St. Prog. Gt	348,257
	66.464	Near Coastal Waters Program	34,194
	66.505	Water Pollution Control - R & D and Demonstration	123,166
	66.701	Toxic Substances Compliance Monitoring Program	158,776
	66.708	Pollution Prevention Incentive Grants Program	13,094
	66.801	Hazardous Waste Management State Program Support	414,969
	66.802	Hazardous Substance Response Trust Fund (Superfund)	241,416
	66.804	State Underground Storage Tanks Program	152,366
	66.805	Leaking Underground Storage Tank Trust Fund Program	781,385
	66.809	Superfund State Core Program Cooperative Agreements	130,666
	66.900	Pollution Prevention Grants Program	58,289
	OFA	Maine Comparative Risk Project Grant	30,960
		Total Department of Environmental Protection	**6,785,406**
Executive Department - State Planning Office			
U.S. Department of Commerce	11.419	Coastal Zone Management Administration Awards	2,774,844
U.S. Department of the Army - Corps of Engineers	12.110	Planning Assistance to States (Section 22)	829
U.S. Department of Defense - Economic Security	12.607	Community Economic Adjustment Planning Assistance	53,012
U.S. Department of Interior - Fish & Wildlife	15.616	Clean Vessel Act	34,445
U.S. Environmental Protection Agency	66.461	Wetlands Protection - State and Tribal Development Grants	56,243
	66.501	Clean Air Research	26,774
	66.504	Solid Waste Disposal Research - Rural Collection Pilot Prog.	23,647
	66.808	Solid Waste Management Assistance	8,377
U.S. Department of Energy	81.039	National Energy Information Center	7,061
Federal Emergency Management Agency	83.105	Community Assistance Program - State Support Services	132,990
Corporation for National and Community Service	94.003	State Commissions	151,330
	94.004	Learn and Serve America - School and Comm. Based Prog.	9,970
	94.006	AmeriCorps	571,840
	94.009	Training and Technical Assistance	65,636
U.S. Department of Energy	OFA	Petroleum Violation Escrow Funds	359,919
		Total Executive Department - State Planning Office	**4,276,917**
Executive Department - Substance Abuse			
U.S. Department of Education	84.186	Safe and Drug-Free Schools and Comm. - State Grants	402,233
U.S. Department of Health and Human Services	93.194	Communities Prevention Coalitions (Partnership) Demo. Gts.	335
	93.902	Model Comp. Drug Abuse Treatment Prog. for Critical Pop.	102,852
	93.950	Capacity Expansion Program	114,345
	OFA	State Prevention Needs Assessment	158,209
U.S. Department of Housing and Urban Develop.	OFA	Innovative Homeless	263,886
		Total Executive Department - Substance Abuse	**1,041,860**
Maine Historic Preservation Commission			
U.S. Department of the Interior	15.904	Historic Preservation Fund Grants In Aid	450,414
		Total Maine Historic Preservation Commission	**450,414**
Maine Historical Records Advisory Council			
National Archives Reference Service	94.090	Advisory Council Training Regrant Project	14,244

State of Maine
Schedule of Federal Financial Assistance
For the Year Ended June 30, 1996

Schedule A (Continued)

Recipient/Grantor Agency	Federal Catalog Number	Program Title	Expenditures 1996
		Non-Major Federal Programs	**$**
		Total Maine Historical Records Advisory Council	**14,244**
Maine Human Rights Commission			
Equal Employment Opportunity Commission	30.002	Employment Discrimination - State/Local Fair Employ. Pract.	185,168
		Total Maine Human Rights Commission	**185,168**
Department of Human Services			
U.S. Department of Agriculture	10.560	State Administrative Expenses for Child Nutrition	201,965
	10.570	Nutrition Program for the Elderly (Commodities) (Note 3C)	712,615
U.S. Department of Justice	16.575	Crime Victim Assistance	609,610
U.S. Department of Labor	17.235	Senior Community Service Employment Program	445,400
U.S. Environmental Protection Agency	66.032	State Indoor Radon Grants	144,627
	66.419	Water Pollution Control - State/Interstate Program Support	59,647
	66.432	State Public Water System Supervision	731,192
	66.xxx	EPA Lead Grant	130,209
Nuclear Regulatory Commission	77.001	Radiation Control-Training Assistance & Adv. Counseling	65,157
U.S. Department of Health and Human Services	93.041	Special Programs for the Aging - Title VII, Chapter 3	16,566
	93.042	Special Programs for the Aging - Title VII, Chapter 2	218,681
	93.043	Special Programs for the Aging - Title III, Part F	90,406
	93.044	Special Programs for the Aging - Title III, Part B	1,604,148
	93.045	Special Programs for the Aging - Title III, Part C	2,535,568
	93.046	Special Programs for the Aging - Title III, Part D	52,461
	93.048	Special Programs for the Aging - Title IV	7,500
	93.049	Special Programs for the Aging - Title VII, Chapter 6	5,464
	93.110	Maternal & Child Health Federal Consolidated Programs	149,812
	93.116	Project Grants & Agreements for TB Control Programs	139,107
	93.130	Primary Care Services - Rescourse Coordination & Dev'l	113,689
	93.165	Grants for State Loan Repayment	35,587
	93.184	Disabilities Prevention	77,748
	93.197	Childhood Lead Poisoning Prevention Projects	331,017
	93.268	Childhood Immunization Grants	1,122,174
	93.393	Cancer Cause and Prevention Research	879,038
	93.554	Emergency Protection Grants - Substance Abuse	63,671
	93.556	Family Preservation and Support Services	282,059
	93.562	Assistance Payments - Research	241,949
	93.566	Refugee and Entrant Assist. - St. Administered Programs	398,187
	93.569	Comm. Svs. B/G - Discret. Awards - Food & Nutrition	2,138,863
	93.575	Payments to States for Child Care Assistance	3,814,531
	93.576	Refugee and Entrant Assistance - Discretionary Grants	125,052
	93.600	Head Start	116,625
	93.614	Child Development Associate Scholarships	5,040
	93.643	Children's Justice Grants to States	21,043
	93.645	Child Welfare Services - State Grants	1,410,497
	93.659	Adoption Assistance	3,495,784
	93.669	Child Abuse and Neglect State Grants	161,945
	93.671	Family Violence Prev. and Svcs. - Grants to States	290,664
	93.673	Grts. to States for Plan. and Develop. of Depend. Care Prog.	44,405
	93.674	Independent Living	636,449

State of Maine
Schedule of Federal Financial Assistance
For the Year Ended June 30, 1996

Schedule A (Continued)

Recipient/Grantor Agency	Federal Catalog Number	Program Title	Expenditures 1996
		Non-Major Federal Programs	**$**
Department of Human Services - continued			
	93.679	Child Abuse Challange Grants	300,114
	93.777	State Survey & Cert. of Health Care Providers and Suppliers	1,732,849
	93.779	Health Care Financing Research, Demo., and Evaluations	468,125
	93.913	Grants to States for Operation of Offices of Rural Health	40,006
	93.917	HIV Care Formula Grants	248,802
	93.919	Coop. Agree. for St. Based Comp. Breast & Cervical Cancer	1,695,157
	93.940	HIV Prevention Activities - Health Deptartment Based	1,421,076
	93.944	Human Immunodeficiency Virus (AIDS) - Surveillance	72,475
	93.977	Preventive Health Services - Sexually Transmitted Diseases	159,351
	93.987	Health Programs for Refugees	11,800
	93.988	Coop. Agreements for State Based Diabetes Control Programs	331,169
	93.991	Preventive Health and Health Services Block Grant	1,845,319
	93.994	Maternal & Child Health Services Block Grant to States	3,806,159
	OFA	Vital Statistics Cooperative Program	479,956
		Total Department of Human Services	**36,338,510**
Department of Inland Fisheries and Wildlife			
U.S. Department of the Interior	15.605	Sport Fish Restoration	1,711,343
	15.611	Wildlife Restoration	2,348,590
	15.612	Rare and Endangered Species Conservation	47,063
	15.617	Wildlife Conservation and Appreciation	21,490
	15.FFC	American Wetlands Conservation Act	578,535
U.S. Department of Transportation	20.005	Boating Safety Financial Assistance	549,333
U.S. Environmental Protection Agency	66.461	Wetlands Protection - State and Tribal Development Grants	16,144
U.S. Department of the Interior	OFA	Colonial Waterbird Inventory	46,999
		Total Department of Inland Fisheries and Wildlife	**5,319,497**
Judicial Department			
U.S. Department of Health & Human Services	93.586	State Court Improvement Program	4,500
		Total Judicial Department	**4,500**
Department of Labor			
U.S. Department of Labor	17.002	Labor Force Statistics	829,474
	17.202	Certification of Foreign Workers for Temp. Employment	1,050,962
	17.245	Trade Adjustment Assistance - Workers	2,325,993
	17.249	Employment Services and Job Training - Pilot Programs	163,388
	17.500	Occupational Safety and Health - 7c1 Agreement	69,532
	17.506	Occupational Safety and Health - 7c1 Agreement	293,485
	17.600	Mine Health and Safety Grants	19,576
	17.801	Disabled Veterans Outreach Program	910,079
	17.802	Veterans Employment Program	489,774
Corporation for National and Community Service	94.001	Defense Conversion Grant	577,999
U.S. Department of Labor	OFA	Me. Occupational Information Coordination Committee	86,949
		Total Department of Labor	**6,817,211**
Maine Health Care Finance Commission			
U.S. Department of Health and Human Services	93.779	Health Care Financing Research, Demo., and Evaluations	79,719

State of Maine
Schedule of Federal Financial Assistance
For the Year Ended June 30, 1996

Schedule A (Continued)

Recipient/Grantor Agency	Federal Catalog Number	Program Title	Expenditures 1996
		Non-Major Federal Programs	**$**
		Total Maine Health Care Finance Commission	**79,719**
Maine State Library			
National Foundation on the Arts and the Humanities	45.149	Promo. of the Humanities - Div. of Preservation and Access	84,886
U.S. Department of Education	84.034	Public Library Services	751,827
	84.154	Public Library Construction & Technology Enhancement	195,265
		Total Maine State Library	**1,031,978**
Maine State Museum			
U.S. Department of the Interior	15.904	Historic Preservation Fund Grants in Aid	28,861
		Total Maine State Museum	**28,861**
Department of Marine Resources			
U.S. Department of Commerce	11.307	Special Econ. Develop. and Adj. Assistance Program	19,410
	11.405	Anadromous Fish Conservation Act Program	47,000
	11.407	Interjurisdictional Fisheries Act of 1986	151,499
	11.427	Fisheries Development & Research & Develop./Coop. Agreem	75,343
U.S. Department of Conservation	11.452	Unallied Industry Projects	41,185
U.S. Department of Commerce	11.474	Atlantic Coastal Fisheries Cooperative Management Act	120,525
U.S. Department of Interior	15.605	Sport Fish Restoration	377,297
U.S. Department of Conservation	OFA	NURP - Patch Dynamics & Reproductive Biology	805
U.S. Department of Health and Human Services	OFA	FDA Sampling Plan Soft Shell Clams & Acid Testing	5,088
		Total Department of Marine Resources	**838,152**
Department of Mental Health and Mental Retardation			
U.S. Department of Housing and Urban Develop.	14.179	Nehemiah Housing Opportunity Grant Program	254,343
	14.238	Shelter Plus Care	367,876
U.S. Department of Health and Human Services	93.104	Comp. Comm. MH Svcs. for Child. w/ Serious Emot. Disturb.	3,632,580
	93.125	Mental Health Planning and Demonstration Projects	196,120
	93.150	Projects for Assistance in Transition from Homelessness	302,331
	93.242	Mental Health Research Grants	55,579
	93.630	Development Disabilities Basic Supp. & Advocacy Grants	347,253
	93.958	Blk Gts for Community Mental Health Services	1,295,413
		Total Department of Mental Health and Mental Retardation	**6,451,495**
Department of Public Safety			
U.S. Department of Justice	16.005	Public Education on Drug Abuse - Information	49,576
	16.579	Byrne Formula Grant Program	2,984,253
	16.580	Edward Byrne Mem. State and Local Law Enforcement	33,272
	16.588	Formula Grants - Violence Against Women	8,147
U.S. Department of Transportation	20.218	Motor Carrier Safety Assistance Program	384,547
	20.600	State and Community Highway Safety	1,416,498
		Total Department of Public Safety	**4,876,293**
Department of State			
U.S. Department of Transportation	20.218	Motor Carrier Safety Assistance Program	64,672
	20.600	State and Community Highway Safety	47,171

State of Maine
Schedule of Federal Financial Assistance
For the Year Ended June 30, 1996

Schedule A (Continued)

Recipient/Grantor Agency	Federal Catalog Number	Program Title	Expenditures 1996
		Non-Major Federal Programs	$
		Total Department of State	**111,843**
Department of Transportation			
U.S. Department of the Army, Corps of Engineers	12.105	Protection of Highways, Highway Bridges, and Pub. Works	66,727
U.S. Department of Housing and Urban Develop.	14.174	HUD 1995 Grant - Sen. George Mitchell	241,190
U.S. Department of Interior	15.145	Indian Business Development Grant Program	435,675
U.S. Department of Transportation	20.106	Airport Improvement Program	28,456
	20.308	Local Rail Freight Assistance	422,838
	20.500	Federal Transit Capital Improvement Grants	957,458
	20.505	Federal Transit Technical Studies Grants	151,565
	20.507	Federal Transit Capital and Operating Assistance Formula Gt	1,562,399
	20.509	Public Transportation for Nonurbanized Areas	1,411,571
	20.514	Transit Planning and Research	37,092
		Total Department of Transportation	**5,314,971**
Total Federal Assistance - Nonmajor Programs:			**122,092,377**
Total Federal Assistance - Major Programs:			**1,161,072,312**
Total Federal Financial Assistance:			**$ 1,283,164,689**

See accompanying Notes to the Schedule of Federal Financial Assistance.

State of Maine

Notes to the Schedule of Federal Financial Assistance

June 30, 1996

1. **Purpose of the Schedule**

   A Schedule of Federal Financial Assistance, showing total expenditures for each Federal financial assistance program as identified in the Catalog of Federal Domestic Assistance (CFDA), has been included for supplementary information. Significant Federal financial assistance programs which have not been assigned a CFDA number have been identified as *Other Federal Assistance (OFA).*

2. **Significant Accounting Policies**

   A. Reporting Entity - The accompanying schedule includes all Federal financial assistance programs of the State of Maine for the fiscal year ended June 30, 1996. The reporting entity is defined in Note 1 to the primary government financial statements.

   B. Basis of Presentation - The information in the accompanying Schedule of Federal Financial Assistance is presented in accordance with OMB Circular A-128.

      1. Federal Financial Assistance - Pursuant to the Single Audit Act of 1984 (Public Law 98-502) and OMB Circular A-128, Federal financial assistance is defined as assistance provided by a Federal agency, either directly or indirectly, in the form of grants, contracts, cooperative agreements, loans, loan guarantees, property, interest subsidies, insurance, or direct appropriations. Accordingly, nonmonetary Federal assistance, including food stamps and food commodities, is included in Federal financial assistance and, therefore, is reported on the Schedule of Federal Financial Assistance. Federal financial assistance does not include direct Federal cash assistance to individuals.

      2. Major and Nonmajor Programs - The Single Audit Act of 1984 and OMB Circular A-128 establish the levels of expenditures or expenses to be used in defining major and nonmajor Federal financial assistance programs. Major programs for the State of Maine were those which exceeded $4 million in expenditures, distributions, or issuances for the fiscal year ended June 30, 1996.

   C. Basis of Accounting - The information presented in the Schedule of Federal Financial Assistance is presented primarily on the cash basis of accounting, which is consistent with the other Federal grant reports. Maine’s primary government financial statements are reported on the modified accrual basis of accounting. Consequently, the schedule’s data may not be directly traceable to the financial statements.

3. **Program Notes**

A. Department of Education - Food Distribution Program (CFDA 10.550): The reported total of Federal financial assistance represents the value of food commodities distributed to various schools, institutions, and other qualifying entities. The value of inventory as of June 30, 1996 was $169,248.

B. Department of Human Services - Food Stamps (CFDA 10.551): The reported total of Federal financial assistance represents the value of food coupons issued. The value of inventory as of June 30, 1996 was $21,850,534.

C. Department of Human Services - Nutrition Program for the Elderly (CFDA 10.570): The amount reported of $712,615 represents cash in lieu of commodities expended in the Elderly Feeding Program.

D. Department of Agriculture - Temporary Emergency Food Assistance - Food Commodities (CFDA 10.569): The reported total of Federal financial assistance consists of administrative costs of $139,369 under the Temporary Food Assistance Program (TEFAP). The value of inventory at June 30, 1996 was $26,932.

Food Commodities for Soup Kitchens (CFDA 10.571): The reported total of Federal financial assistance consists of $521,245 the value of food commodities distributed under the Food Commodities for Soup Kitchens Program. The value of inventory at June 30, 1996 was $279,498.

E. Department of Administrative and Financial Services - Donated Federal Surplus Personal Property (CFDA 39.003): Distributions are reported at fair market value. The value of inventory as of June 30, 1996 was $434,923.

F. Department of Labor - Unemployment Insurance (CFDA 17.225): Reported expenditures are comprised of the following:

Emergency Unemployment Compensation	$	(190,784)
U.I. Administrative Grant		14,918,346
Extended Benefits		(12,101)
Unemployment Compensation for Ex-service Personnel		1,241,076
Unemployment Compensation for Federal Employees		860,047
Trade Readjustment Act (FUBA)		2,569,511
Unemployment Compensation for Ex-postal Workers		255,400
NAFTA Trade Training		14,773
Disaster Unemployment Assistance		(2,911)
Unemployment Insurance - Reemployment		256,038
Total	$	19,909,395

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STATE OF MAINE

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Independent Auditor's Report on Internal Control Structure Based on an Audit of Primary Government Financial Statements Performed in Accordance With *Government Auditing Standards*

To the President of the Senate and the
Speaker of the House of Representatives

We have audited the primary government financial statements of the State of Maine, as of and for the year ended June 30, 1996, and have issued our qualified report thereon dated March 31, 1997.

We conducted our audit in accordance with generally accepted auditing standards and *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 primary government financial statements are free of material misstatement.

The management of the State of Maine is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

In planning and performing our audit of the primary government financial statements of the State of Maine for the year ended June 30, 1996, we obtained an understanding of the internal control structure. With respect to the internal control structure, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk in order to determine our auditing procedures for the purpose of expressing our opinion on the primary government financial statements and not to provide an opinion on the internal control structure. Accordingly, we do not express such an opinion.

We noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the primary government financial statements.

Reportable conditions other than material weaknesses that we found and the State agencies to which they relate are identified in the accompanying Schedule of Reportable Conditions.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the primary government financial statements 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 structure would not necessarily disclose all matters in the internal control structure that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. However, we noted the following matters involving the internal control structure and its operation that we consider to be material weaknesses as defined above. These conditions were considered in determining the nature, timing, and extent of the procedures to be performed in our audit of the financial statements of the State of Maine, for the year ended June 30, 1996.

(A) Department of Administrative and Financial Services

<u>Finding</u>: Insufficient procedures and resources for external financial reporting

The Department of Administrative and Financial Services (DAFS) has not established procedures, and has insufficient resources, to reasonably fulfill its responsibilities for external financial reporting. Title 5, MRSA § 281, established DAFS as the principal fiscal department of State government. As such, it is responsible for coordinating financial planning and programming activities of all departments and agencies. DAFS, through the Bureau of Accounts and Control, prepares the official annual financial report of the State.

Although DAFS has initiated action to address previously reported deficiencies regarding capital leases, a closing package and fixed assets, among others, the benefits of those actions will not be realized for some time. DAFS is insufficiently staffed to provide the financial accounting guidance necessary to fulfill its legal responsibilities. To ensure timely completion and development of all required elements, additional resources need to be assigned to the annual financial report.

<u>Recommendation</u>:

We recommend that DAFS commit additional resources to the financial reporting process.

<u>Auditee Response</u>:

We concur with this audit finding. Although the Department has made substantial progress in addressing previously reported deficiencies in the areas of capital leases, a closing package and fixed assets, we concur that additional resources must be committed to the financial reporting process, including the establishment of a strong CAFR team in the Bureau of Accounts and Control. This is a high priority for the Department, and we will take appropriate steps during FY 98 to ensure these resources are available.

(B) Department of Administrative and Financial Services

<u>Finding:</u> External payment interface disbursements of $15.3 million were not recorded in the State's financial records

The external payment interface disbursement system is used to efficiently process a majority of the State's disbursements. State agencies create payment voucher records that are subjected to system edits and are then "run" (interfacing with the State's automated accounting system, MFASIS) to generate checks for the payment vouchers.

Procedures have not yet been established to ensure that all "interface payments" are recorded in the proper fiscal year. An audit adjustment of $15.3 million was necessary to reflect these interface payments ($2 million in the General Fund, $13.3 million in the Special Revenue Fund).

<u>Recommendation:</u>

We recommend that procedures be implemented to ensure that the "external interface payments" are recorded on the State's financial records in the proper fiscal year.

<u>Auditee Response:</u>

We concur.

(C) Department of Administrative and Financial Services

Finding: Fixed asset records incomplete (Prior Year Finding)

Title 5, MRSA § 1742, requires the Bureau of General Services to maintain a current inventory of all land, buildings and equipment. During fiscal year 1996, the Bureau of General Services did not have detailed records of all land, buildings and equipment owned by the State. As a result, the State's financial statements do not include the General Fixed Assets Account Group, which is required to be presented to conform with Generally Accepted Accounting Principles (GAAP). This omission resulted in a qualified audit opinion.

Accurate records for the General Fixed Asset Account Group are necessary for financial reporting and reducing the risk of misappropriated State property.

Recommendation:

We recommend that the Department of Administrative and Financial Services ensure that inventories are current as required by State law. Upon completion of a statewide inventory, fixed asset records can be established for financial reporting and control purposes.

Auditee Response:

We agree with the auditor's recommendation. In fiscal year 1997, the law changed and the Bureau of Accounts and Control (Bureau) assumed responsibility for maintaining the fixed asset records of the state. Currently, the Bureau is in the process of installing an automated system which will address accounting and financial reporting for fixed assets. This project is expected to be completed by November, 1998.

(D) Department of Administrative and Financial Services

Finding: Inadequate internal control system in place to identify capital leases (Prior Year Finding)

The Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards (SFAS) No. 13, Accounting for Leases, defines capital and operating leases, the criteria for classifying each type of lease, and the accounting, reporting and financial statement disclosures required by lessees and lessors.

The Department of Administrative and Financial Services (DAFS) does not evaluate and report leases in accordance with SFAS No. 13. Centralized information is not sufficient to prepare all necessary financial adjustments and required note disclosures. DAFS classifies all leases entered into by the State as operating leases without any documented basis to support the classification.

Rental Property Leases

We were unable to evaluate rental property leases in accordance with SFAS No. 13 due to insufficient records maintained by the State. Future minimum lease payments for these leases are approximately $9.8 million in the governmental funds and $31.4 million in the Internal Service Fund. The amount of the adjustments that would be necessary if these leases were evaluated is not known. In our opinion, it is material.

Office Equipment Leases

Future minimum lease payments for equipment leases are approximately $5.5 million in the governmental funds and $4.2 million in the Internal Service Fund. The amount of the adjustments that would be necessary if these leases were evaluated is not known.

Recommendation:

We recommend that DAFS develop and implement procedures to evaluate and record all leases in accordance with SFAS Accounting No. 13.

Auditee Response:

Several months ago we contracted with Brian S. Berry & Associates, CPAs to categorize all existing leases, and write procedures for agencies to follow for future lease transactions. Working with BGS staff, the project is moving along as planned and the database is being built to accommodate equipment and capital leases. A CPA from Accounts and Control is also involved in this project and is satisfied with the results to date. Compliance with FASB No. 13 is the anticipated outcome.

(E) Department of Administrative and Financial Services

Finding: No independent verification of lottery data from vendor (Prior Year Finding)

The Bureau of Alcoholic Beverages and Lottery Operations (BABLO) contracts with two vendors for specialized services relating to instant ticket and on-line sales. During fiscal year ended June 30, 1996, instant ticket sales totaled approximately $98 million and on-line sales totaled approximately $50 million; 65 percent and 33 percent of lottery revenue, respectively. BABLO relies almost entirely on information provided by the vendors to record sales, prize expense, commissions expense, accounts receivable and prizes payable. In addition, BABLO uses vendor reports to advise the bank of the amount of cash to be swept from agents' accounts for deposit to the State Treasury.

Lottery operations are dependent on the vendors' computer systems both for data processing and ticket validation. Financial statements are derived almost entirely from vendor reports. BABLO has not independently verified whether the instant ticket vendor system correctly records, processes, summarizes and report financial data.

BABLO has contracted with an independent auditor to conduct an audit in accordance with Statements on Auditing Standards (SAS) 70, *Report on the Processing of Transactions by Service Organizations*, for the instant lottery vendor. To date, that engagement has not been completed.

Recommendation:

We recommend that the Bureau of Alcoholic Beverages and Lottery Operations require the vendor to obtain and provide a SAS 70 audit. The requirement should include independent assurance, each fiscal year, that the vendors' control environments include properly designed policies and procedures, and those policies are placed in operation and produce reliable data.

Auditee Response:

We agree with the recommendation of the auditor and have at the State's expense contracted with a qualified firm to conduct the SAS 70. In the future we will require our vendors to provide us with the SAS 70 report at their own expense.

We also noted other matters involving the internal control structure and its operation that we will report to the management of the State of Maine, in a separate letter dated July 18, 1997.

This report is intended for the information of management, the Legislature, and those Federal agencies that provided financial assistance. However, this report is a matter of public record and its distribution is not limited.

Gail M. Chase
State Auditor

March 31, 1997

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Independent Auditor's Report on the Internal Control Structure Used in Administering Federal Financial Assistance Programs

To the President of the Senate and the
Speaker of the House of Representatives

We have audited the primary government financial statements of the State of Maine, as of and for the year ended June 30, 1996, and have issued our qualified report thereon dated March 31, 1997. We have also audited the compliance of the State of Maine with requirements applicable to major Federal financial assistance programs and have issued our report thereon dated July 18, 1997.

We conducted our audits in accordance with generally accepted auditing standards; *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Circular A-128, *Audits of State and Local Governments*. Those standards and OMB Circular A-128 require that we plan and perform the audit to obtain reasonable assurance about whether the primary government financial statements are free of material misstatement and about whether the State of Maine complied with laws and regulations, noncompliance with which would be material to a major Federal financial assistance program.

In planning and performing our audits for the year ended June 30, 1996, we considered the internal control structure of the State of Maine in order to determine our auditing procedures for the purpose of expressing our opinions on the primary government financial statements of the State of Maine, and on the compliance of the State of Maine with requirements applicable to major programs, and to report on the internal control structure in accordance with OMB Circular A-128. This report addresses our consideration of internal control structure policies and procedures relevant to compliance with requirements applicable to Federal financial assistance programs. We have addressed internal control structure policies and procedures relevant to our audit of the primary government financial statements in a separate report dated March 31, 1997.

The management of the State of Maine is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of primary government financial statements in accordance with generally accepted accounting principles, and that Federal financial assistance programs are managed in compliance with applicable laws and regulations. Because of inherent limitations in any internal control structure, errors, irregularities, or instances of noncompliance may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

For the purpose of this report, we have classified the significant internal control structure policies and procedures used in administering Federal financial assistance programs in the following categories:

<u>Accounting Controls</u>

- Budget
- Cash/cash receipts
- Revenue and receivables
- Expenditures for goods and services and accounts payable
- Payroll and related liabilities
- Inventories
- Property, equipment, and capital expenditures

<u>Administrative Controls</u>

General Requirements

- Political activity
- Davis-Bacon Act
- Civil rights
- Cash management
- Relocation assistance and real property acquisition
- Federal financial reports
- Allowable costs/cost principles
- Drug-free Workplace Act
- Administrative requirements

Specific Requirements

- Types of services allowed or not allowed
- Eligibility
- Matching, level of effort, or earmarking
- Reporting
- Cost allocation
- Special requirements, if any
- Monitoring subrecipients

Claims for advances and reimbursements

Amounts claimed or used for matching

For all major programs and for nonmajor programs on a cyclical basis as described in the following paragraph, we obtained an understanding of the design of relevant policies and procedures for the internal control structure categories listed in the preceding paragraph, we determined whether they have been placed in operation, and we assessed control risk.

Because of the large number of nonmajor programs and the decentralized administration of these programs, we performed procedures to obtain an understanding of the internal control structure policies and procedures relevant to nonmajor programs on a cyclical basis. Our procedures during the current year covered 27 percent of the nonmajor programs administered by the State of Maine. The nonmajor programs not covered during the current year have been or are expected to be subject to such procedures at least once during the three year cycle.

During the year ended June 30, 1996, the State of Maine expended 91 percent of its total Federal financial assistance under major Federal financial assistance programs.

We performed tests of controls, as required by OMB Circular A-128, to evaluate the effectiveness of the design and operation of internal control structure policies and procedures that we considered relevant to preventing or detecting material noncompliance with specific requirements, general requirements, and requirements governing claims for advances and reimbursements and amounts claimed or used for matching that are applicable to each of the State of Maine's major Federal financial assistance programs, which are identified in the accompanying Schedule of Federal Financial Assistance. Our procedures were less in scope than would be necessary to render an opinion on these internal control structure policies and procedures. Accordingly, we do not express such an opinion.

We noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the State of Maine's ability to administer Federal financial assistance programs in accordance with applicable laws and regulations.

Reportable conditions other than material weaknesses that we found and the State agencies to which they relate are identified in the accompanying Schedule of Reportable Conditions.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control structure elements does not reduce to a relatively low level the risk that noncompliance with laws and regulations that would be material to a Federal financial assistance program 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 structure policies and procedures used in administering federal financial assistance would not necessarily disclose all matters in the internal control structure that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. However, we noted the following matter involving the internal control structure and its operation that we consider to be a material weakness as defined above. This condition was considered in determining the nature, timing, and extent of the procedures to be performed in our audit of the compliance of the State of Maine with requirements applicable to its major Federal financial assistance programs for the year ended June 30, 1996, and this report does not affect our report thereon dated July 18, 1997.

(F) Office of the Treasurer of State

Various Federal Programs
CFDA# Various **Questioned Costs:** None

Finding: Internal control not adequate to ensure compliance with Cash Management Improvement Act

The Office of the Treasurer of State (Treasurer) is responsible for administering the Cash Management Improvement Act (CMIA) for the State of Maine. In this capacity, the Treasurer is responsible for the negotiation of the annual Cash Management Improvement Act (Agreement) between the State of Maine and the Secretary of the Treasury, United States Department of the Treasury for the preparation of the Annual Report on CMIA, and for monitoring State agency compliance with CMIA provisions.

Inadequate internal control procedures resulted in the following instances of noncompliance with CMIA provisions:

- Three Federal assistance programs (Child and Adult Care Food Program, Payments to State for Child Care Assistance Program, and the Disaster Assistance Program) were omitted when the State implemented cash management procedures required by CMIA. As a result, no drawdown methods were designated, nor interest calculations made for these programs, resulting in a potential interest obligation to the Federal government. According 31 CFR Subpart A, Section 205.4, the CMIA, "applies, at a minimum to all programs that meet the threshold for major Federal assistance programs in a state. . ." unless otherwise exempted in the Agreement. The three programs were not exempted, and therefore should have been addressed.

- According to the CMIA Policy and Procedures Manual, the Treasurer is responsible for certain central oversight procedures, which include analyses of monthly interest liability reports and periodic reviews of agency cash management records. The Treasurer did not analyze monthly interest liability reports nor periodically review agency cash management records. As a result, monthly interest liability reports, used to prepare the CMIA Annual Report, were incomplete. In addition, certain State agencies did not maintain cash management records sufficient to document compliance with established drawdown methods.

- The Treasurer is required to calculate and report State and Federal interest liability to the Federal government via the CMIA Annual Report. Interest calculations must be made in accordance with 31 CFR Part 205 and the Agreement. The report included interest calculation errors which resulted from incorrect assumptions being made when preparing the report. The effect of the errors was to overstate the State's interest liability for the Food Stamp Administration Program and to understate the State's interest liability for the administrative costs for the Medical Assistance Program, Social Security Disability Insurance Program and the Community Development Block Grant Program resulting in an additional State interest liability of $4,479.

Recommendation:

1. The Treasurer should include all applicable Federal assistance programs in its cash management procedures.

2. We recommend that the Treasurer implement oversight procedures to assure full compliance with the provisions of the CMIA. This should include periodic reviews of agency cash management records for all Federal programs subject to the CMIA.

3. We recommend that the Treasurer file a revised report for the 1996 fiscal year and pay the U.S. Treasury $4,479. In addition, the Treasurer should ensure that all data used in the preparation of the CMIA Annual Report is appropriate.

Auditee Response:

1. *The programs are to be included if they are over the threshold limit of $4,000,000. A review will be done to include them in the tracking of Federal funds. The Program 10.558 is in the FY 1998 program as well as 93.525 Child Care Adult Food Program and Child Care Assistance.*

2. *Periodic reviews by Treasury personnel for FY 1997 were done by memo correspondence. The contract for FY 1998 hopefully will contain some personal contact. Perhaps the Treasurer can ask for additional funding to obtain funds to allow for contract personnel to conduct audits of procedures utilized by departments.*

3. *The Contractor hired to calculate the Interest Liability Report did not include Administrative Cost in the Program Nos. 93.778, 93.560, 93.802 and 14.228 and All Cost in 10.561. The calculations in November 1997 will include the corrections and will be filed so noted. Internal controls will be noted to revise all calculations to be certain the proper accounts are included in the CMIA filing. The Contractor has been advised by the Auditor in charge of the Treasury Audit of this finding and will also be so advised by the Office of the State Treasurer.*

We also noted other matters involving the internal control structure and its operation that we will report to the management of the State of Maine in a separate letter dated July 18, 1997.

This report is intended for the information of management, the Legislature, and those Federal agencies that provided financial assistance. However, this report is a matter of public record and its distribution is not limited.

Gail M. Chase
State Auditor

July 18, 1997

Schedule B

STATE OF MAINE
SCHEDULE OF REPORTABLE CONDITIONS
FOR THE YEAR ENDED JUNE 30, 1996

DEPARTMENT OF ADMINISTRATIVE AND FINANCIAL SERVICES

(1) Bureau of Accounts and Control

Various Federal Programs
CFDA # Various — Questioned Costs: $639,000

Finding: Excess balance of $4.9 million in Retiree Health Insurance Fund

The State of Maine provides health care benefits for most retirees using the pay-as-you-go method. Funds for post retirement health care benefits are generated by current employer contributions for State employees, Maine Technical College employees, and an appropriation to cover 25% of the costs for teachers. Public Laws 1995, Chapter 368, Subsection G-3 and G-4 repealed the provision that required payment by the Maine State Retirement System for retirees' health insurance premiums.

The Department of Administrative and Financial Services subsequently assumed administrative responsibility for post retirement health care insurance premium payments. Effective July 1, 1995, contributions were collected and deposited to Trust and Agency Fund (074) Retiree Health Insurance. Despite the transfer of responsibility, the Maine State Retirement System continued to make premium payments to the insurance carrier, on behalf of the State of Maine, for several months in State fiscal year 1995, in order to reduce an existing balance. As a result, the State had an excess balance of $4.9 million in the Retiree Health Insurance Fund as of June 30, 1996, of which $639,000 was attributable to excess contributions from Federal programs.

Contributions to the fund were made at the rate of 3.8%, which was later reduced, for a six month period, to .53% for State employees but not for the Maine Technical College employees. As a result, the Maine Technical College paid an approximate $400,000 in excess contributions as of June 30, 1996. In July, 1996, the rate increased to 5.08% for all participants.

Office of Management and Budget Circular A-87, *Cost Principles for State, Local, and Indian Tribal Governments*, states that for post retirement health benefits (PRHB) financed on a pay-as-you-go method, allowable costs will be limited to those representing payments to retirees or their beneficiaries and, in the current year, PRHB costs must be paid either to: (a) an insurer or other benefit provider as current year costs or premiums, or (b) an insurer or trustee to maintain in a trust fund or reserve for the sole purpose of providing post retirement health benefits to retirees and other beneficiaries.

Recommendation:

We recommend the following:

1. That the contributions for retiree health insurance be accounted for in an internal service fund;
2. That excess contributions be returned to the Maine Technical College System;
3. That the current balance in the fund be reduced to comply with the pay-as-you-go requirements of A-87; and
4. That the Federal government be reimbursed $639,000 in questioned costs in the event that the excess balance is not reduced.

Auditee Response:

We agree with recommendation 1, that the fund was set up incorrectly; a code change will immediately correct the error and all subsequent reports will indicate that this is an Internal Service Fund.

2, 3, and 4, we will be having discussions with the Bureau of Employee Health, who administers this program, to bring it into compliance. This was the first year that the State administered this program and, consequently, there are adjustments in procedures that must be made.

(2) Bureau of Accounts and Control

Finding: Inadequate financial closing procedures

The State Controller's year-end financial closing procedures are inadequate to record all expenditures and accounts payable. Although during the first 60 days of each fiscal year the Pre-Audit Division reviews all invoices over $250 to ensure proper recording, we noted that 14 of 47 governmental fund transactions tested were not properly reported. Of the 14, 12 were over $250 and should have been detected by the Pre-Audit review.

We also noted two transactions, totaling $935,000, that should have been recorded in the Capital Projects Fund.

Recommendation:

To ensure that the State's financial statements properly reflect all significant accounts payable and expenditures, we recommend that the State Controller accrue all on-line disbursements, and provide specific instructions and training to all State agencies regarding year-end closing procedures.

Auditee Response:

We agree with this finding but we hope that in closing FY 97 we will do a better job. The Pre-Audit unit has been made aware of this finding and will be trying to do a better job. The agencies have been notified about accrual coding, but we cannot be sure if the information reaches the individuals that do the coding. If Pre-Audit does a better job it should not be a problem.

DEPARTMENT OF EDUCATION

(3) Support Systems Team Construction/Transportation Subteam

Finding: General Fund school construction money expended with inadequate oversight (Prior Year Finding)

The State Board of Education has procedures in place to review new construction projects, but after the concept approval process, its oversight essentially ends. The Department of Education (DOE) does not have adequate control procedures in place over fiscal decisions affecting approved projects. One individual has sole authority to approve or reject changes to school construction plans and specifications, requests for additional moveable equipment, and the use of unexpended funds after project completion. In addition, there are no specific written criteria used to approve the requested changes or the use of unexpended funds. In fiscal year 1996, the Board approved $37.6 million for 12 school construction projects.

DEPARTMENT OF EDUCATION

Recommendation:

We recommend that DOE provide greater oversight over school construction projects. DOE should develop and document policies and procedures that include criteria for approval or rejection of projects.

Auditee Response:

The Department of Education, through agency restructuring undertaken during the fiscal year 1996, has reviewed and reassigned oversight functions within the school construction program. Previously, the program was managed by one (1) specialist. Department restructuring resulted in the creation of the position of Policy Director/Team Leader for the school construction program and the 117th Legislature created a second specialist position for the program.

The State Board of Education Standing Committee for School Construction also now reviews all matters of funding related to school construction projects, prior to full Board consideration of approval.

Governor King has appointed a commission on school facilities for the purpose of reviewing all policy, procedures, and rules related to school construction with the charge to advance legislation and recommended substantive rule changes, by December 1, 1997, pertinent to all school construction matters, including oversight and responsibilities. This Commission will include representation from the Bureau of General Services, which has a role in approving allowable costs associated with school construction.

DEPARTMENT OF HUMAN SERVICES

(4) Office of Management and Budget
Division of Financial Services

Finding: General Fund not reimbursed for $982,320 in expenditures (Prior Year Finding)

Title 19 MRSA § 514 requires ". . .all collections, fees, and incentive payments received by the Department of Human Services (DHS) from child support collections to be dedicated to reduce the State's share of Aid to Families with Dependent Children (AFDC) and to cover the costs of making collections."

During the 1996 fiscal year, DHS transferred $2,654,000 of incentive revenue to the Special Revenue fund to cover the cost of collecting child support payments. DHS incurred collection costs of $1,671,680 in the Special Revenue Fund. As a result, incentive revenue transferred to the Special Revenue Fund exceeded actual collection costs by $982,320.

Recommendation:

In order to ensure that revenue transfers do not exceed the cost of making child support collections, we recommend that DHS review its accounting procedures regarding the handling of the $2,654,000. We further recommend that DHS immediately use the $982,320 to offset the General Fund's share of the AFDC program and to cover the cost of making child support collections.

Auditee Response:

The Department of Human Services (DHS) disagrees with this auditors interpretation of Title 19 MRSA § 514. The department has incurred collection costs in excess of $2,654,000. in the general fund and dedicated fund account (0100).

DHS will review accounting procedures regarding the handling of the $2,654,000. DHS will reduce the eligible amount to be transferred in Fiscal Year 1998 by $982,320.

(5) Office of Management and Budget
Division of Financial Services

Finding: General Fund due $823,160 (Prior Year Finding)

The Department of Human Services (DHS) accumulates incentive funds along with child support collections in the same dedicated revenue account. The revenue is credited to one reporting organization code while the related expenditures are charged to various other reporting organization codes, all within the same account.

Title 19 MRSA § 514 requires "... all collections, fees, and incentive payments received by the Department of Human Services (DHS) from child support collections to be dedicated to reduce the State's share of Aid to Families with Dependent Children (AFDC) and to cover the costs of making collections."

DHS incorrectly reimbursed the Federal account, rather than the General Fund, with $823,160 of incentive funds for AFDC benefit payments.

DEPARTMENT OF HUMAN SERVICES

Transfers involving incentive revenues and child support collections are complex, and the current accounting system does not facilitate tracking those revenues and their related expenditure.

Recommendation:

We recommend that the General Fund recoup the $823,160 from the Federal account to properly reflect the correct fund balance for incentive funds.

We also recommend that DHS - Division of Financial Services record the receipt and disbursement of the incentive funds in the same reporting organization code.

Auditee Response:

The Department of Human Services (DHS) concurs with the above audit finding. DHS will prepare a journal to recoup the $823,160 from the Federal account.

DHS will also review the process now in place to determine if changes may be implemented to simplify a very complex system.

DEPARTMENT OF LABOR

(6) Bureau of Employment Security
Division of Unemployment Compensation

Finding: Inadequate internal control and accounting procedures for the Employment Security Trust Fund taxes receivable balance (Prior Year Finding)

An entity's internal control structure consists of the policies and procedures established to provide reasonable assurance that specific entity objectives will be achieved. Entity objectives should include adequate safeguards over access to and use of assets and records, accurate and reliable accounting data, segregation of duties, proper authorization of transactions and activities, independent checks on performance, and proper valuation of recorded amounts. Establishing and maintaining an internal control structure is an important management responsibility. In order to provide reasonable assurance that an entity's objectives will be achieved, the internal control structure should be under ongoing supervision by management to assure that it is operating as intended and that it is modified as appropriate for changes in conditions.

Internal controls at the Division of Unemployment Compensation (Division) are deficient as follows:

1. Nonreconciliation of Unemployment Compensation Tax receivable reports

   The Division generates two unemployment compensation tax reports. One report is used to track delinquencies and the other is the basis for the tax receivable balance reflected on the State's accounting records. The Division does not reconcile the receivable balances of the two reports.

2. Inadequate allowance account for uncollectible receivables

   At June 30, 1996, the Division has established an allowance account of $2.9 million for estimated uncollectible taxes receivable. This amount consisted only of the amount necessary to actually write off uncollectible balances. It did not include any estimate of other amounts that might not be collected. For financial reporting purposes, an audit adjustment of $3.6 million was proposed and accepted.

3. No systematic, formal procedures exist for selection of account write-offs

   A listing of receivable balances deemed to be uncollectible by the Division is compiled annually and submitted to the Department of Administrative and Financial Services for approval to be written off. The Division uses no formal criteria to determine which accounts should be written off. Only those employers who communicate their inability to pay their receivable balances to the Division are considered for write-off; all other receivable balances remain outstanding. As not all receivable balances are reviewed and considered for elimination, potential write-offs are overlooked and the reserve for uncollectible balances is understated at year-end.

Recommendation:

We recommend that the Division:

1. Reconcile the delinquency report and the TXAM report at least annually;

2. Develop and document procedures to establish an allowance account for uncollectible receivables in accordance with generally accepted accounting principles, and maintain documentation of the methodology and calculation; and

3. Establish criteria to be used to determine uncollectible taxes receivable.

Auditee Response:

1. *The Unemployment compensation tax accounts receivable delinquency report is a billing report and the TXAM report is used by the Office of Administrative Services as a*

statement of debt on file. The Bureau does not bill for all debts on file, therefore the two reports do not reconcile.

2. *Completion date has been extended until resources become available to develop procedures for estimation of a reserve for uncollectible receivables.*

3. *The Bureau has developed formal criteria to determine account write offs and will annually review all receivable balances to consider for elimination.*

(7) Bureau of Employment Security
Division of Unemployment Compensation

Finding: No procedures to establish an allowance account for uncollectible receivables (Prior Year Finding)

The Division of Unemployment Compensation (Division) does not establish an allowance account for uncollectible receivables as required by generally accepted accounting principles (GAAP).

The benefit overpayments receivable balance was $6.7 million at June 30, 1996. An adjustment of $5.3 million was necessary to establish the allowance account for those account balances estimated to be uncollectible.

Recommendation:

We recommend that the Division develop procedures to establish an allowance account for uncollectible receivables in accordance with GAAP and maintain documentation of methodology and calculation.

Auditee Response:

The UI 0475 report and benefits overpayment detail aging have been reconciled each month since April 1996.

Management is currently in the process of obtaining relevant and reliable data to be used in developing a methodology for estimating a reserve for uncollectible receivables. The reserve for uncollectibles will be developed in accordance with the provisions of FASB #5, "Accounting for Contingencies". It is anticipated this procedure will be in place in or about January 1, 1998.

(8) Office of Administrative Services

Finding: Revenue recognition criteria not observed

The Office of Administrative Services records the accounts receivable balance for the Unemployment Compensation Trust Fund on the State's official accounting records annually. All receivables that have not been deemed uncollectible and posted to the reserve for uncollectible accounts are automatically considered to be deferred revenue and are recorded as such. No analysis is performed on the year-end receivable balance or subsequent collections to determine whether any of the deferred revenue ($9.8 million) should be classified as revenue as of June 30, 1996. An audit adjustment of $7.7 million was necessary.

Governmental Accounting and Financial Reporting Standards, Section 1600.106 states that revenues are to be recognized in the accounting period in which they become susceptible to accrual and when they become collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. The State has further defined "soon enough thereafter" by adopting a policy of considering any collections made on receivables within 60 days after fiscal year end as revenue for the old fiscal year. The Office of Administrative Services' current practices do not comply with revenue recognition criteria as prescribed by the Governmental Accounting Standards Board (GASB).

Recommendation:

We recommend that the Office of Administrative Services comply with GASB revenue recognition criteria and implement procedures to ensure that revenue is recognized in the proper period.

Auditee Response:

The Office of Administrative Services performs a quarterly analysis to determine what portion of revenues currently classified as deferred revenue should be classified as revenue. The analysis identifies the receivables collected for the two months following the last quarterly adjustment to the Controller's records. This is used to determine the percentage of collections to outstanding receivables that should be classified as revenue. The analysis is performed for unemployment taxes, less doubtful and bankruptcies, and penalty and interest.

No action is being taken to reclassify deferred revenue as revenue on the controller's records as it distorts the balances on the Appropriations revenue received and available cash balance in the MFASIS on line screens and B919 reports. The interest and penalty receivables classified as revenues would appear as excess cash in the Special Administrative Expense Fund and, by law, any amount in excess of $100-thousand remaining in the Fund must be transferred to the U.C. Trust Fund as of June 30 of each year.

(9) Division of Reimbursement

Finding: Patient care and treatment services not billed, untimely recording of revenues and subsidiary accounts not maintained

Internal control over billings, and recording of revenues and receivables, at the Department of Mental Health and Mental Retardation (DMHMR), Division of Reimbursements, is deficient as follows :

1. Services not billed

   DMHMR had not billed the Department of Human Services - Medicaid for case management services provided from March through June, 1996. General Fund revenues and receivables were understated by approximately $1.4 million at June 30, 1996. DMHMR has one year from the date of service to bill Medicaid, or reimbursement will be denied.

2. Untimely recording of revenues / receivables

   DMHMR did not establish a receivable at the time of billing for services provided by the Bureau of Children with Special Needs (BCSN) and for Crisis Intervention services, due primarily to the automated system's inability to process the volume of transactions. Also, receivables were not established at the time claims were billed to Medicare. Billing for these services was a few to several months later than the date the services were provided. Revenue was recorded at the time payment was received by DMHMR and, consequently, was not recognized in the proper accounting period.

   The Government Accounting Standards Board Codification, Sec. 1600.106, states that revenues should be recorded when susceptible to accrual, and collectibility can be reasonably estimated.

   The amount of unrecorded revenue and receivables attributable to BCSN and Crisis Intervention services was estimated at $360,000 at June 30, 1996. The amount of unrecorded revenue and receivables attributable to Medicare claims was indeterminate.

3. Individual subsidiary receivable accounts not maintained

   DMHMR did not maintain individual subsidiary receivable accounts for crisis intervention and case management services, due to limitations of the automated system. Therefore, the aggregate collections and outstanding balance of accounts receivable could not be reconciled to individual receivable amounts.

Recommendation:

We recommend that DMHMR:

1. Bill and record accounts receivable on a timely basis and record an appropriate offset for uncollectible amounts,

2. Maintain subsidiary receivable accounts, and

3. Advise the State Controller of all revenue and receivables, to ensure recording in the correct fiscal year.

Auditee Response:

In response to your audit of Accounts Receivable Reconciliation for FY 1996, the Department of Mental Health, Mental Retardation & Substance Abuse Services is responding to the three areas as outlined.

1. *Services Not Billed: The Department is currently working with DHS to enter the information directly into their system thereby catching the Department up to the point that the State will not lose funding. In addition, the Department will be working with DHS for implementing a new system that would allow the regions to bill directly for these services.*

2. *Untimely Recording of Revenues/Receivables: The Reimbursement Division has been behind because of the old system of billing and tracking, and we are working with DHS and the Controller's Office to rectify this problem. As soon as DHS catches the Department up for case management we will examine what else their system might be able to do for us including the accounts receivable piece.*

3. *Individual Subsidiary Receivable Accounts Not Maintained: When the Department gets current on their billing we will be working with DHS to see if the system they have has an accounts receivable portion to it. One of the concerns that the Department has for the Medicaid only bills is that the point of entry the Department will be able to tell if the individual can be billed to Medicaid. If the individual is a Medicaid client, it may not make sense to set it up as a receivable as long as we have a system of matching collections. The maintaining of receivables for individuals at the facilities is a more realistic approach because these clients have different types of billing mechanisms available that would include multiple sources of funds.*

DEPARTMENT OF TRANSPORTATION

(10) Bureau of Finance and Administration

Finding: Internal controls insufficient to ensure compliance with budgetary statutes

Title 5 M.R.S.A. § 1543 states, “No money shall be drawn from the State Treasury, except in accordance with appropriations duly authorized by law.” Additionally, § 1585 states, “Any balance of any appropriation . . .made by the legislature for any state department. . .which at any time may not be required for the purpose named in such appropriations. . .may be transferred. . to any other appropriation. . .for the use of the same department. . .subject to the review of the joint standing committee of the Legislature having jurisdiction over appropriations and financial affairs.”

In order to facilitate day-to-day financial operations, the Maine Department of Transportation (MDOT) routinely transfers previously charged expenditures from one appropriation account to another. This process allows MDOT to charge current expenditures to the account from which earlier expenditures were transferred without exceeding that account’s allotment. These temporary transfers are made via journal voucher containing the description “to correct,” “to adjust,” or “to reverse” errors in previous transactions. These descriptions are misleading, as the original expenditures were appropriately charged. The journals are made so frequently that MDOT uses a control number to monitor and restore the amounts transferred.

MDOT’s action’s resulted in the:

1. Creation of allotment without specific Legislative approval, thus circumventing legal restrictions;
2. Potential for misstatement of financial statements due to the timing of transactions;
3. Inadequate budgetary controls; and
4. Inability to accurately forecast budgetary needs.

In July, 1995, journaled amounts had been substantially restored to the original appropriation account.

Recommendation:

We recommend that MDOT comply with statutes governing the appropriation and expenditure of State funds. We further recommend that MDOT seek the advise of the State Controller and the State Budget Officer.

DEPARTMENT OF TRANSPORTATION

Auditee Response:

The Maine Department of Transportation concurs with the recommendation of the State Audit Department and will investigate with the Office of the State Controller and the State Budget Office, any and all opportunities to increase the efficiency and effectiveness of the financial operations of the Maine Department of Transportation.

OFFICE OF THE TREASURER OF STATE

(11) Finding: Inadequate internal control and accounting procedures over trust and agency funds (Prior Year Finding)

An entity's internal control structure consists of the policies and procedures established to provide reasonable assurance that specific entity objectives will be achieved. Establishing and maintaining an internal control structure is an important management responsibility. To provide reasonable assurance that an entity's objectives will be achieved, the internal control structure should be under ongoing supervision by management to determine that it is operating as intended and that it is modified as appropriate for changes in conditions.

We reviewed the Office of the Treasurer of State's (Treasurer) internal control system for trust and agency funds and found the following deficiencies:

1. Private Trust Fund subsidiary ledgers not reconciled or do not exist

   The Private Trust Fund consists of various deposits and guaranty funds which are held by the Treasurer for safekeeping. The Treasurer maintains subsidiary ledgers for two of the guaranty funds, but does not reconcile the ledgers to the State's official accounting records. A review of the funds identified mispostings in the Insurance Guaranty Fund and the Maine Employment Security Compensation Guaranty Fund. Further, the Treasurer does not maintain a subsidiary ledger that supports the balance in the Treasurer's Safekeeping Fund, which was $1.78 million as of June 30, 1996.

2. Detailed accounting data for state-held trust funds not provided to Controller

   The Treasurer is responsible for recording any activity within state-held trust funds. The current practice is to record transactions only within trust fund equity accounts, if recorded at all. Operating accounts are not used. Consequently, detailed operating account activity that the Controller needs for preparing accurate operating statements is not available.

As a result, adjustments were required at year-end to correctly reflect income, expenditure and investment balances relative to the trust funds.

Recommendation:

We again recommend that the Treasurer strengthen internal controls to provide reasonable assurance that specific objectives are achieved. To accomplish this, the following policies and procedures should be implemented:

1. Maintain subsidiary ledgers for all individual funds within the Private Trust Fund for which the Treasurer has custodial responsibilities and reconcile these ledgers to the State's official accounting system at least annually so that year-end balances are reported correctly; and

2. Provide the State Controller with State-held trust fund activity information to post on operating accounts of the State's accounting system.

Auditee Response:

1. *Control ledgers can be set up with a figure entered reflecting the balance of all accounts and the balance to the Controller can be worked upon to balance.*

2. *Journals providing purchases and sales which change the balances of the three State Trust Funds contain specific detail of each transaction as to cost, proceeds and gain/loss. These journals are on file in the Controller's Office. Activity in the income portion is reported monthly when income is received net of bank management fees and treasury will look into recording this differently to properly reflect the fee expense.*

(12) Finding: Deposits in transit not recorded at year-end

A reconciliation of cash balances at June 30, 1996, performed by the Office of the Treasurer of State (Treasurer), identified $3.6 million of deposits in transit. These amounts represent bank deposits for which no cash receipt statements had been recorded. The $3.6 million was therefore not recorded on the balance sheet at June 30, 1996.

Recommendation:

We recommend that the Treasurer identify deposits in transit at year-end, determine the funds to which they will be recorded and provide the information to the State Controller to report in accordance with Generally Accepted Accounting Principles.

Auditee Response:

The Controller's Office and the Treasurer's Office are working on a paperless cash receipt program which will immediately enter deposits into the Accounting System eliminating this Audit Exception. Bids and the dollars needed to effect this system hopefully will be available in the 1998 Legislative Session.

Presently the Treasurer has requested timely presentation of cash receipts but as the State Auditor notes not all agencies respond with timely presentation.

Schedule B

STATE OF MAINE
SCHEDULE OF REPORTABLE CONDITIONS
FOR THE YEAR ENDED JUNE 30, 1996

DEPARTMENT OF ADMINISTRATIVE AND FINANCIAL SERVICES

(1) Bureau of Accounts and Control

Various Federal Programs
CFDA # Various — Questioned Costs: $639,000

Finding: Excess balance of $4.9 million in Retiree Health Insurance Fund

The State of Maine provides health care benefits for most retirees using the pay-as-you-go method. Funds for post retirement health care benefits are generated by current employer contributions for State employees, Maine Technical College employees, and an appropriation to cover 25% of the costs for teachers. Public Laws 1995, Chapter 368, Subsection G-3 and G-4 repealed the provision that required payment by the Maine State Retirement System for retirees' health insurance premiums.

The Department of Administrative and Financial Services subsequently assumed administrative responsibility for post retirement health care insurance premium payments. Effective July 1, 1995, contributions were collected and deposited to Trust and Agency Fund (074) Retiree Health Insurance. Despite the transfer of responsibility, the Maine State Retirement System continued to make premium payments to the insurance carrier, on behalf of the State of Maine, for several months in State fiscal year 1995, in order to reduce an existing balance. As a result, the State had an excess balance of $4.9 million in the Retiree Health Insurance Fund as of June 30, 1996, of which $639,000 was attributable to excess contributions from Federal programs.

Contributions to the fund were made at the rate of 3.8%, which was later reduced, for a six month period, to .53% for State employees but not for the Maine Technical College employees. As a result, the Maine Technical College paid an approximate $400,000 in excess contributions as of June 30, 1996. In July, 1996, the rate increased to 5.08% for all participants.

Office of Management and Budget Circular A-87, *Cost Principles for State, Local, and Indian Tribal Governments,* states that for post retirement health benefits (PRHB) financed on a pay-as-you-go method, allowable costs will be limited to those representing payments to retirees or their beneficiaries and, in the current year, PRHB costs must be paid either to: (a) an insurer or other benefit provider as current year costs or premiums, or (b) an insurer or trustee to maintain in a trust fund or reserve for the sole purpose of providing post retirement health benefits to retirees and other beneficiaries.

Recommendation:

We recommend the following:

1. That the contributions for retiree health insurance be accounted for in an internal service fund;
2. That excess contributions be returned to the Maine Technical College System;
3. That the current balance in the fund be reduced to comply with the pay-as-you-go requirements of A-87; and
4. That the Federal government be reimbursed $639,000 in questioned costs in the event that the excess balance is not reduced.

Auditee Response:

We agree with recommendation 1, that the fund was set up incorrectly; a code change will immediately correct the error and all subsequent reports will indicate that this is an Internal Service Fund.

2, 3, and 4, we will be having discussions with the Bureau of Employee Health, who administers this program, to bring it into compliance. This was the first year that the State administered this program and, consequently, there are adjustments in procedures that must be made.

(2) Bureau of Accounts and Control

Finding: Inadequate financial closing procedures

The State Controller's year-end financial closing procedures are inadequate to record all expenditures and accounts payable. Although during the first 60 days of each fiscal year the Pre-Audit Division reviews all invoices over $250 to ensure proper recording, we noted that 14 of 47 governmental fund transactions tested were not properly reported. Of the 14, 12 were over $250 and should have been detected by the Pre-Audit review.

We also noted two transactions, totaling $935,000, that should have been recorded in the Capital Projects Fund.

Recommendation:

To ensure that the State's financial statements properly reflect all significant accounts payable and expenditures, we recommend that the State Controller accrue all on-line disbursements, and provide specific instructions and training to all State agencies regarding year-end closing procedures.

Auditee Response:

We agree with this finding but we hope that in closing FY 97 we will do a better job. The Pre-Audit unit has been made aware of this finding and will be trying to do a better job. The agencies have been notified about accrual coding, but we cannot be sure if the information reaches the individuals that do the coding. If Pre-Audit does a better job it should not be a problem.

DEPARTMENT OF EDUCATION

(3) Support Systems Team Construction/Transportation Subteam

Finding: General Fund school construction money expended with inadequate oversight (Prior Year Finding)

The State Board of Education has procedures in place to review new construction projects, but after the concept approval process, its oversight essentially ends. The Department of Education (DOE) does not have adequate control procedures in place over fiscal decisions affecting approved projects. One individual has sole authority to approve or reject changes to school construction plans and specifications, requests for additional moveable equipment, and the use of unexpended funds after project completion. In addition, there are no specific written criteria used to approve the requested changes or the use of unexpended funds. In fiscal year 1996, the Board approved $37.6 million for 12 school construction projects.

DEPARTMENT OF EDUCATION

Recommendation:

We recommend that DOE provide greater oversight over school construction projects. DOE should develop and document policies and procedures that include criteria for approval or rejection of projects.

Auditee Response:

The Department of Education, through agency restructuring undertaken during the fiscal year 1996, has reviewed and reassigned oversight functions within the school construction program. Previously, the program was managed by one (1) specialist. Department restructuring resulted in the creation of the position of Policy Director/Team Leader for the school construction program and the 117th Legislature created a second specialist position for the program.

The State Board of Education Standing Committee for School Construction also now reviews all matters of funding related to school construction projects, prior to full Board consideration of approval.

Governor King has appointed a commission on school facilities for the purpose of reviewing all policy, procedures, and rules related to school construction with the charge to advance legislation and recommended substantive rule changes, by December 1, 1997, pertinent to all school construction matters, including oversight and responsibilities. This Commission will include representation from the Bureau of General Services, which has a role in approving allowable costs associated with school construction.

DEPARTMENT OF HUMAN SERVICES

(4) Office of Management and Budget
Division of Financial Services

Finding: General Fund not reimbursed for $982,320 in expenditures (Prior Year Finding)

Title 19 MRSA § 514 requires ". . .all collections, fees, and incentive payments received by the Department of Human Services (DHS) from child support collections to be dedicated to reduce the State's share of Aid to Families with Dependent Children (AFDC) and to cover the costs of making collections."

During the 1996 fiscal year, DHS transferred $2,654,000 of incentive revenue to the Special Revenue fund to cover the cost of collecting child support payments. DHS incurred collection costs of $1,671,680 in the Special Revenue Fund. As a result, incentive revenue transferred to the Special Revenue Fund exceeded actual collection costs by $982,320.

<u>Recommendation</u>:

In order to ensure that revenue transfers do not exceed the cost of making child support collections, we recommend that DHS review its accounting procedures regarding the handling of the $2,654,000. We further recommend that DHS immediately use the $982,320 to offset the General Fund's share of the AFDC program and to cover the cost of making child support collections.

<u>Auditee Response</u>:

The Department of Human Services (DHS) disagrees with this auditors interpretation of Title 19 MRSA § 514. The department has incurred collection costs in excess of $2,654,000. in the general fund and dedicated fund account (0100).

DHS will review accounting procedures regarding the handling of the $2,654,000. DHS will reduce the eligible amount to be transferred in Fiscal Year 1998 by $982,320.

(5) Office of Management and Budget
Division of Financial Services

<u>Finding</u>: General Fund due $823,160 (Prior Year Finding)

The Department of Human Services (DHS) accumulates incentive funds along with child support collections in the same dedicated revenue account. The revenue is credited to one reporting organization code while the related expenditures are charged to various other reporting organization codes, all within the same account.

Title 19 MRSA § 514 requires ". . . all collections, fees, and incentive payments received by the Department of Human Services (DHS) from child support collections to be dedicated to reduce the State's share of Aid to Families with Dependent Children (AFDC) and to cover the costs of making collections."

DHS incorrectly reimbursed the Federal account, rather than the General Fund, with $823,160 of incentive funds for AFDC benefit payments.

Transfers involving incentive revenues and child support collections are complex, and the current accounting system does not facilitate tracking those revenues and their related expenditure.

Recommendation:

We recommend that the General Fund recoup the $823,160 from the Federal account to properly reflect the correct fund balance for incentive funds.

We also recommend that DHS - Division of Financial Services record the receipt and disbursement of the incentive funds in the same reporting organization code.

Auditee Response:

The Department of Human Services (DHS) concurs with the above audit finding. DHS will prepare a journal to recoup the $823,160 from the Federal account.

DHS will also review the process now in place to determine if changes may be implemented to simplify a very complex system.

DEPARTMENT OF LABOR

(6) Bureau of Employment Security
Division of Unemployment Compensation

Finding: Inadequate internal control and accounting procedures for the Employment Security Trust Fund taxes receivable balance (Prior Year Finding)

An entity's internal control structure consists of the policies and procedures established to provide reasonable assurance that specific entity objectives will be achieved. Entity objectives should include adequate safeguards over access to and use of assets and records, accurate and reliable accounting data, segregation of duties, proper authorization of transactions and activities, independent checks on performance, and proper valuation of recorded amounts. Establishing and maintaining an internal control structure is an important management responsibility. In order to provide reasonable assurance that an entity's objectives will be achieved, the internal control structure should be under ongoing supervision by management to assure that it is operating as intended and that it is modified as appropriate for changes in conditions.

Internal controls at the Division of Unemployment Compensation (Division) are deficient as follows:

1. Nonreconciliation of Unemployment Compensation Tax receivable reports

   The Division generates two unemployment compensation tax reports. One report is used to track delinquencies and the other is the basis for the tax receivable balance reflected on the State's accounting records. The Division does not reconcile the receivable balances of the two reports.

2. Inadequate allowance account for uncollectible receivables

   At June 30, 1996, the Division has established an allowance account of $2.9 million for estimated uncollectible taxes receivable. This amount consisted only of the amount necessary to actually write off uncollectible balances. It did not include any estimate of other amounts that might not be collected. For financial reporting purposes, an audit adjustment of $3.6 million was proposed and accepted.

3. No systematic, formal procedures exist for selection of account write-offs

   A listing of receivable balances deemed to be uncollectible by the Division is compiled annually and submitted to the Department of Administrative and Financial Services for approval to be written off. The Division uses no formal criteria to determine which accounts should be written off. Only those employers who communicate their inability to pay their receivable balances to the Division are considered for write-off; all other receivable balances remain outstanding. As not all receivable balances are reviewed and considered for elimination, potential write-offs are overlooked and the reserve for uncollectible balances is understated at year-end.

Recommendation:

We recommend that the Division:

1. Reconcile the delinquency report and the TXAM report at least annually;

2. Develop and document procedures to establish an allowance account for uncollectible receivables in accordance with generally accepted accounting principles, and maintain documentation of the methodology and calculation; and

3. Establish criteria to be used to determine uncollectible taxes receivable.

Auditee Response:

1. *The Unemployment compensation tax accounts receivable delinquency report is a billing report and the TXAM report is used by the Office of Administrative Services as a*

statement of debt on file. The Bureau does not bill for all debts on file, therefore the two reports do not reconcile.

2. *Completion date has been extended until resources become available to develop procedures for estimation of a reserve for uncollectible receivables.*

3. *The Bureau has developed formal criteria to determine account write offs and will annually review all receivable balances to consider for elimination.*

(7) Bureau of Employment Security
Division of Unemployment Compensation

Finding: No procedures to establish an allowance account for uncollectible receivables (Prior Year Finding)

The Division of Unemployment Compensation (Division) does not establish an allowance account for uncollectible receivables as required by generally accepted accounting principles (GAAP).

The benefit overpayments receivable balance was $6.7 million at June 30, 1996. An adjustment of $5.3 million was necessary to establish the allowance account for those account balances estimated to be uncollectible.

Recommendation:

We recommend that the Division develop procedures to establish an allowance account for uncollectible receivables in accordance with GAAP and maintain documentation of methodology and calculation.

Auditee Response:

The UI 0475 report and benefits overpayment detail aging have been reconciled each month since April 1996.

Management is currently in the process of obtaining relevant and reliable data to be used in developing a methodology for estimating a reserve for uncollectible receivables. The reserve for uncollectibles will be developed in accordance with the provisions of FASB #5, "Accounting for Contingencies". It is anticipated this procedure will be in place in or about January 1, 1998.

(8) Office of Administrative Services

Finding: Revenue recognition criteria not observed

The Office of Administrative Services records the accounts receivable balance for the Unemployment Compensation Trust Fund on the State's official accounting records annually. All receivables that have not been deemed uncollectible and posted to the reserve for uncollectible accounts are automatically considered to be deferred revenue and are recorded as such. No analysis is performed on the year-end receivable balance or subsequent collections to determine whether any of the deferred revenue ($9.8 million) should be classified as revenue as of June 30, 1996. An audit adjustment of $7.7 million was necessary.

Governmental Accounting and Financial Reporting Standards, Section 1600.106 states that revenues are to be recognized in the accounting period in which they become susceptible to accrual and when they become collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. The State has further defined "soon enough thereafter" by adopting a policy of considering any collections made on receivables within 60 days after fiscal year end as revenue for the old fiscal year. The Office of Administrative Services' current practices do not comply with revenue recognition criteria as prescribed by the Governmental Accounting Standards Board (GASB).

Recommendation:

We recommend that the Office of Administrative Services comply with GASB revenue recognition criteria and implement procedures to ensure that revenue is recognized in the proper period.

Auditee Response:

The Office of Administrative Services performs a quarterly analysis to determine what portion of revenues currently classified as deferred revenue should be classified as revenue. The analysis identifies the receivables collected for the two months following the last quarterly adjustment to the Controller's records. This is used to determine the percentage of collections to outstanding receivables that should be classified as revenue. The analysis is performed for unemployment taxes, less doubtful and bankruptcies, and penalty and interest.

No action is being taken to reclassify deferred revenue as revenue on the controller's records as it distorts the balances on the Appropriations revenue received and available cash balance in the MFASIS on line screens and B919 reports. The interest and penalty receivables classified as revenues would appear as excess cash in the Special Administrative Expense Fund and, by law, any amount in excess of $100-thousand remaining in the Fund must be transferred to the U.C. Trust Fund as of June 30 of each year.

(9) Division of Reimbursement

Finding: Patient care and treatment services not billed, untimely recording of revenues and subsidiary accounts not maintained

Internal control over billings, and recording of revenues and receivables, at the Department of Mental Health and Mental Retardation (DMHMR), Division of Reimbursements, is deficient as follows :

1. Services not billed

   DMHMR had not billed the Department of Human Services - Medicaid for case management services provided from March through June, 1996. General Fund revenues and receivables were understated by approximately $1.4 million at June 30, 1996. DMHMR has one year from the date of service to bill Medicaid, or reimbursement will be denied.

2. Untimely recording of revenues / receivables

   DMHMR did not establish a receivable at the time of billing for services provided by the Bureau of Children with Special Needs (BCSN) and for Crisis Intervention services, due primarily to the automated system's inability to process the volume of transactions. Also, receivables were not established at the time claims were billed to Medicare. Billing for these services was a few to several months later than the date the services were provided. Revenue was recorded at the time payment was received by DMHMR and, consequently, was not recognized in the proper accounting period.

   The Government Accounting Standards Board Codification, Sec. 1600.106, states that revenues should be recorded when susceptible to accrual, and collectibility can be reasonably estimated.

   The amount of unrecorded revenue and receivables attributable to BCSN and Crisis Intervention services was estimated at $360,000 at June 30, 1996. The amount of unrecorded revenue and receivables attributable to Medicare claims was indeterminate.

3. Individual subsidiary receivable accounts not maintained

   DMHMR did not maintain individual subsidiary receivable accounts for crisis intervention and case management services, due to limitations of the automated system. Therefore, the aggregate collections and outstanding balance of accounts receivable could not be reconciled to individual receivable amounts.

Recommendation:

We recommend that DMHMR:

1. Bill and record accounts receivable on a timely basis and record an appropriate offset for uncollectible amounts,

2. Maintain subsidiary receivable accounts, and

3. Advise the State Controller of all revenue and receivables, to ensure recording in the correct fiscal year.

Auditee Response:

In response to your audit of Accounts Receivable Reconciliation for FY 1996, the Department of Mental Health, Mental Retardation & Substance Abuse Services is responding to the three areas as outlined.

1. *Services Not Billed: The Department is currently working with DHS to enter the information directly into their system thereby catching the Department up to the point that the State will not lose funding. In addition, the Department will be working with DHS for implementing a new system that would allow the regions to bill directly for these services.*

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DEPARTMENT OF TRANSPORTATION

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Finding: Internal controls insufficient to ensure compliance with budgetary statutes

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Recommendation:

We recommend that MDOT comply with statutes governing the appropriation and expenditure of State funds. We further recommend that MDOT seek the advise of the State Controller and the State Budget Officer.

DEPARTMENT OF TRANSPORTATION

Auditee Response:

The Maine Department of Transportation concurs with the recommendation of the State Audit Department and will investigate with the Office of the State Controller and the State Budget Office, any and all opportunities to increase the efficiency and effectiveness of the financial operations of the Maine Department of Transportation.

OFFICE OF THE TREASURER OF STATE

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Recommendation:

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Auditee Response:

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Recommendation:

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Auditee Response:

The Controller's Office and the Treasurer's Office are working on a paperless cash receipt program which will immediately enter deposits into the Accounting System eliminating this Audit Exception. Bids and the dollars needed to effect this system hopefully will be available in the 1998 Legislative Session.

Presently the Treasurer has requested timely presentation of cash receipts but as the State Auditor notes not all agencies respond with timely presentation.

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STATE OF MAINE

DEPARTMENT OF AUDIT

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Independent Auditor's Report on Compliance Based on an Audit of Primary Government Financial Statements Performed in Accordance With *Government Auditing Standards*

To the President of the Senate and the
Speaker of the House of Representatives

We have audited the primary government financial statements of the State of Maine, as of and for the year ended June 30, 1996, and have issued our qualified report thereon dated March 31, 1997.

We conducted our audit in accordance with generally accepted auditing standards and *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 primary government financial statements are free of material misstatement.

Compliance with laws, regulations, contracts, and grants applicable to the State of Maine is the responsibility of the State of Maine's management. As part of obtaining reasonable assurance about whether the primary government financial statements are free of material misstatement, we performed tests of the State of Maine's compliance with certain provisions of laws, regulations, contracts, and grants. However, the objective of our audit of the primary government financial statements was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance that are required to be reported herein under *Government Auditing Standards*.

We noted certain immaterial instances of noncompliance that we will report to the management of the State of Maine in a separate letter dated July 18, 1997.

This report is intended for the information of management, the Legislature, and those Federal agencies that provided financial assistance. However, this report is a matter of public record and its distribution is not limited.

Gail M. Chase
State Auditor

March 31, 1997

STATE OF MAINE

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Independent Auditor's Report on Compliance With the General Requirements Applicable to Federal Financial Assistance Programs

To the President of the Senate and the
Speaker of the House of Representatives

We have audited the primary government financial statements of the State of Maine, as of and for the year ended June 30, 1996, and have issued our qualified report thereon dated March 31, 1997.

We have applied procedures to test the State of Maine's compliance with the following requirements applicable to its Federal financial assistance programs, which are identified in the Schedule of Federal Financial Assistance, for the year ended June 30, 1996:

- Political activity
- Davis-Bacon Act
- Civil rights
- Cash management
- Relocation assistance and real property acquisition
- Federal financial reports
- Allowable costs/cost principles
- Drug-free Workplace Act
- Administrative requirements

Our procedures were limited to the applicable procedures described in the Office of Management and Budget's *Compliance Supplement for Single Audits of State and Local Governments.* Our procedures were substantially less in scope than an audit, the objective of which is the expression of an opinion on the State of Maine's compliance with the requirements listed in the preceding paragraph. Accordingly, we do not express such an opinion.

Material instances of noncompliance consist of failures to follow the general requirements that caused us to conclude that the misstatements resulting from those failures are material to Federal programs. The results of our tests of compliance disclosed the following material instance of noncompliance.

(G) Office of the Treasurer of State

Various Federal Programs
CFDA# Various

Questioned Costs: None

Finding: Internal control not adequate to ensure compliance with Cash Management Improvement Act

The Office of the Treasurer of State (Treasurer) is responsible for administering the Cash Management Improvement Act (CMIA) for the State of Maine. In this capacity, the Treasurer is responsible for the negotiation of the annual Cash Management Improvement Act (Agreement) between the State of Maine and the Secretary of the Treasury, United States Department of the Treasury for the preparation of the Annual Report on CMIA, and for monitoring State agency compliance with CMIA provisions.

Inadequate internal control procedures resulted in the following instances of noncompliance with CMIA provisions:

- Three Federal assistance programs (Child and Adult Care Food Program, Payments to State for Child Care Assistance Program, and the Disaster Assistance Program) were omitted when the State implemented cash management procedures required by CMIA. As a result, no drawdown methods were designated, nor interest calculations made for these programs, resulting in a potential interest obligation to the Federal government. According 31 CFR Subpart A, Section 205.4, the CMIA, "applies, at a minimum to all programs that meet the threshold for major Federal assistance programs in a state. . ." unless otherwise exempted in the Agreement. The three programs were not exempted, and therefore should have been addressed.

- According to the CMIA Policy and Procedures Manual, the Treasurer is responsible for certain central oversight procedures, which include analyses of monthly interest liability reports and periodic reviews of agency cash management records. The Treasurer did not analyze monthly interest liability reports nor periodically review agency cash management records. As a result, monthly interest liability reports, used to prepare the CMIA Annual Report, were incomplete. In addition, certain State agencies did not maintain cash management records sufficient to document compliance with established drawdown methods.

- The Treasurer is required to calculate and report State and Federal interest liability to the Federal government via the CMIA Annual Report. Interest calculations must be made in accordance with 31 CFR Part 205 and the Agreement. The report included interest calculation errors which resulted from incorrect assumptions being made when preparing the report. The effect of the errors was to overstate the State's interest liability for the Food Stamp Administration Program and to understate the State's interest liability for the administrative costs for the Medical Assistance Program, Social Security Disability

Insurance Program and the Community Development Block Grant Program resulting in an additional State interest liability of $4,479.

Recommendation:

1. The Treasurer should include all applicable Federal assistance programs in its cash management procedures.

2. We recommend that the Treasurer implement oversight procedures to assure full compliance with the provisions of the CMIA. This should include periodic reviews of agency cash management records for all Federal programs subject to the CMIA.

3. We recommend that the Treasurer file a revised report for the 1996 fiscal year and pay the U.S. Treasury $4,479. In addition, the Treasurer should ensure that all data used in the preparation of the CMIA Annual Report is appropriate.

Auditee Response:

1. *The programs are to be included if they are over the threshold limit of $4,000,000. A review will be done to include them in the tracking of Federal Funds. The Program 10.558 is in the FY 1998 program as well as 93.525 Child Care Adult Food Program and Child Care Assistance.*

2. *Periodic reviews by Treasury personnel for FY 1997 were done by memo correspondence. The contract for FY 1998 hopefully will contain some personal contact. Perhaps the Treasurer can ask for additional funding to obtain funds to allow for contract personnel to conduct audits of procedures utilized by departments.*

3. *The Contractor hired to calculate the Interest Liability Report did not include Administrative Cost in the Program Nos. 93.778, 93.560, 93.802 and 14.228 and All Cost in 10.561. The calculations in November 1997 will include the corrections and will be filed so noted. Internal controls will be noted to revise all calculations to be certain the proper accounts are included in the CMIA filing. The Contractor has been advised by the Auditor in charge of the Treasury Audit of this finding and will also be so advised by the Office of the State Treasurer.*

We considered this material instance of noncompliance in forming our opinion on whether the State of Maine's 1996 primary government financial statements are presented fairly, in all material respects, in conformity with generally accepted accounting principles, and this report does not affect our report dated March 31, 1997, on those financial statements.

Except as described above, the results of our procedures to determine compliance indicate that, with respect to the items tested, the State of Maine complied, in all material respects, with the requirements listed in the second paragraph of this report. With respect to items not tested, nothing came to our attention that caused us to believe that the State of Maine had not complied, in all material respects, with those requirements. However, the results of our procedures also disclosed immaterial instances of noncompliance with those requirements, which are described in the accompanying Schedule of Findings and Questioned Costs.

This report is intended for the information of management, the Legislature, and those Federal agencies that provided financial assistance. However, this report is a matter of public record and its distribution is not limited.

Gail M. Chase
State Auditor

July 18, 1997

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Independent Auditor's Report on Compliance With Specific Requirements Applicable to Major Federal Financial Assistance Programs

To the President of the Senate and the
Speaker of the House of Representatives

We have audited the primary government financial statements of the State of Maine, as of and for the year ended June 30, 1996, and have issued our qualified report thereon dated March 31, 1997.

We have also audited the State of Maine's compliance with the requirements governing types of services allowed or unallowed; eligibility; matching, level of effort, or earmarking; reporting; cost allocation; monitoring subrecipients; claims for advances and reimbursements; and amounts claimed or used for matching that are applicable to each of its major Federal financial assistance programs, which are identified in the accompanying Schedule of Federal Financial Assistance, for the year ended June 30, 1996. The management of the State of Maine is responsible for the State of Maine's compliance with those requirements. Our responsibility is to express an opinion on compliance with those requirements based on our audit.

We conducted our audit of compliance with those requirements in accordance with generally accepted auditing standards; *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Circular A-128, *Audits of State and Local Governments*. Those standards and OMB Circular A-128 require that we plan and perform the audit to obtain reasonable assurance about whether material noncompliance with the requirements referred to above occurred. An audit includes examining, on a test basis, evidence about the State of Maine's compliance with those requirements. We believe that our audit provides a reasonable basis for our opinion.

The results of our audit procedures disclosed that the State of Maine did not comply with the matching, level of effort, or earmarking requirements of the Substance Abuse Prevention and Treatment Block Grant, as described below. In our opinion, the maintenance of effort and allocation of grant funds received from the Substance Abuse Prevention and Treatment Block Grant is necessary for the State of Maine to comply with the requirements applicable to that major program.

(H) Executive Department

Substance Abuse Prevention and
Treatment Block Grant
CFDA# 93.959

Questioned Costs: None

Finding: Failure to meet maintenance of effort requirement for State fiscal year 1996

Title 42 USC 300x.30 requires the Maine Office of Substance Abuse (MOSA) to demonstrate maintenance of effort (MOE), consisting of State expenditures at a level no less than the average expenditures of the previous two years. In fiscal year 1996, MOSA did not satisfy the MOE requirement by $630,251.

Recommendation:

We recommend that MOSA consult with appropriate State and Federal officials to reach a mutually acceptable solution.

Auditee Response:

Failure to meet the maintenance of effort requirement for SFY 1996 was reported by the Office of Substance Abuse in its FFY 1997 Block Grant application. In August 1996 the Office submitted a written request seeking guidance and consideration in obtaining a waiver for the maintenance of effort requirements. In January 1997 the Office submitted a written request for additional discussion for the purpose of exploring feasible alternatives in resolving this issue. In April and in May 1997 the director had a series of meetings with a number of individuals within the Substance Abuse and Mental Health Services Administration (SAMHSA) regarding the State of Maine's maintenance of effort issue. During the course of these meetings, it was noted that Maine had not considered Medicaid match for substance abuse services which were in the Mental Health Division's account as funds which could be counted toward complying with the maintenance of effort requirements.

On May 23, 1997, a financial order was written to transfer $630,000 from the Division of Mental Health's Medicaid match account to the Office of Substance Abuse for use as match for substance abuse services. The effects of the transfer are that OSA has control over the Medicaid allocation and use of these funds for services the Office wishes to support. It was agreed that this funding effort would continue and thus be included in complying with the maintenance of effort requirements.

(I) Executive Department

Substance Abuse Prevention and

Treatment Block Grant

<u>CFDA#</u> 93.959

<u>Questioned Costs</u>: None

<u>Finding</u>: Grant management procedures are not sufficient to ensure compliance with expenditure requirements

Federal funds are received by the Maine Office of Substance Abuse (MOSA) for the Substance Abuse Prevention and Treatment Block Grant. Approximately 85% of the funds are passed to subrecipients to carry out the purposes of the grant.

Grant funds of $180,300 were obligated to, but not spent by, subrecipients at the end of the second year of the grant, in violation of grant requirements. Grant funds that were required to be set aside for specific purposes (42 USC 300 x22) fell short of the required amounts by $285,700, which is material to the program.

MOSA is subject to Federal sanctions until adequate procedures are established to properly administer the grant.

<u>Recommendation</u>:

We recommend that MOSA timely allocate funds to subrecipients so that they may expend funds as required. We also recommend that MOSA improve the accounting system to support monitoring of expenditures and required set-aside allocations for each specific block grant award.

<u>Auditee Response</u>:

The Office of Substance reported in its FFY 1997 Federal Block Grant application that the State failed to meet the set-aside requirement for pregnant women and women with dependent children. A major reason for not meeting the requirement was due to the fact that this was a new set-aside requirement and the Office lacked sufficient staff to quickly implement it. Other reasons include a Request for Proposal procedure mandated by State Statute, late startup on the part of new community programs, and off-cycle contracts. We expect to have contract cycles changed to an "on cycle" schedule (7/1 - 6/30) to coincide with the SFY and allow use of state accounting systems for accurate tracking and documentation.

As previously noted, the Office of Substance Abuse will implement two accounting systems to track set-asides, obligations, and expenditures. This will enable the office to monitor activity in a much more accurate and accessible manner and allow us to detect potential issues well in advance and allow sufficient time for corrective action.

Again, due to the loss of staff, performance of subrecipient contracts was not consistent with the hiring of a full-time staff person, performance for subrecipient contracts funded during FFY 1997 will be vigorously monitored. Performance reports will be produced quarterly and staff of the treatment division will consistently track performance.

Obligations will be planned three months in advance prior to implementation and thereby provide adequate time for subrecipient contracts to make expenditures within the allowed period. In addition, with the implementation of the new accounting systems, contract officers and fiscal staff will be able to monitor set-aside expenditures more accurately and frequently.

The results of our audit procedures disclosed immaterial instances of noncompliance with the requirements referred to above, which are described in the accompanying Schedule of Findings and Questioned Costs. We considered these instances of noncompliance in forming our opinion on compliance, which is expressed in the following paragraph.

In our opinion, except for those instances of noncompliance with the requirements applicable to the Substance Abuse Prevention and Treatment Block Grant referred to in the fourth paragraph of this report, the State of Maine complied, in all material respects, with the requirements governing types of services allowed or unallowed; eligibility; matching, level of effort, or earmarking; reporting; cost allocation; monitoring subrecipients; claims for advances and reimbursements; and amounts claimed or used for matching that are applicable to each of its major Federal financial assistance programs for the year ended June 30, 1996.

This report is intended for the information of management, the Legislature, and those Federal agencies that provided financial assistance. However, this report is a matter of public record and its distribution is not limited.

Gail M. Chase
State Auditor

July 18, 1997

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Independent Auditor's Report on Compliance With Specific Requirements Applicable to Nonmajor Federal Financial Assistance Program Transactions

To the President of the Senate and the
Speaker of the House of Representatives

We have audited the primary government financial statements of the State of Maine, as of and for the year ended June 30, 1996, and have issued our qualified report thereon dated March 31, 1997.

In connection with our audit of the primary government financial statements of the State of Maine, and with our consideration of the State of Maine's control structure used to administer Federal financial assistance programs, as required by Office of Management and Budget (OMB) Circular A-128, *Audits of State and Local Governments*, we selected certain transactions applicable to certain nonmajor Federal financial assistance programs for the year ended June 30, 1996. As required by OMB Circular A-128, we have performed auditing procedures to test compliance with the requirements governing types of services allowed or unallowed; eligibility; and subrecipient monitoring that are applicable to those transactions. Our procedures were substantially less in scope than an audit, the objective of which is the expression of an opinion on the State of Maine's compliance with these requirements. Accordingly, we do not express such an opinion.

With respect to the items tested, the results of those procedures disclosed no material instances of noncompliance with the requirements listed in the preceding paragraph. With respect to items not tested, nothing came to our attention that caused us to believe that the State of Maine had not complied, in all material respects, with those requirements. However, the results of our procedures disclosed immaterial instances of noncompliance with those requirements, which are described in the accompanying Schedule of Findings and Questioned Costs.

This report is intended for the information of management, the Legislature, and those Federal agencies that provided financial assistance. However, this report is a matter of public record and its distribution is not limited.

Gail M. Chase
State Auditor

July 18, 1997

STATE OF MAINE
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 1996

DEPARTMENT OF ADMINISTRATIVE AND FINANCIAL SERVICES

(13) Bureau of Accounts and Control

Various Federal Programs
CFDA # Various — Questioned Costs: None

Finding: No system to communicate changes in regulations

Title 5 MRSA § 281 states that the Department of Administrative and Financial Services (DAFS) is the principal fiscal department of State government. DAFS is responsible for coordinating financial planning and programming activities of departments and agencies of State government and for preparing and reporting financial data and statistics to the Governor and to the Legislature.

There is no system in place to ensure knowledge of, or to advise State personnel of, new Federal regulations. All State administered, Federally funded programs must comply with Office of Management and Budget Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments*. Although this Circular was revised in May, 1995, to become effective September 1, 1995, many State accounting personnel had no knowledge of the change. Noncompliance may result in an obligation to the Federal government.

We noted the following instances where State agencies were not following payroll recordkeeping requirements in accordance with the new Circular:

- Department of Human Services - periodic certifications of time charges not completed
- Department of Education - Division of Vocational Rehabilitation Services - appropriate time records not maintained
- Department of Education - Division of Applied Technology - time charged based on budgetary estimates

Recommendation:

We recommend that the DAFS develop a system that will ensure that any changes in Federal regulations, which have statewide implications, be communicated to affected agencies.

Auditee Response:

A new half time CPA will be assigned, among others, the tasks mentioned in this finding, specifically federal regulations. She will follow OMB, GASB, and other federal agencies and associations that impact the State's financial compliance and management. Additionally, she will be checking the Federal Register for competitive grant opportunities, alerting the appropriate agency. Communicating new developments and regulations to the proper state sources will be the CPA's responsibility.

(14) Bureau of Accounts and Control

Various Federal Programs
CFDA # Various Questioned Costs**:** $639,000

Finding: Excess balance of $4.9 million in Retiree Health Insurance Fund

Text of finding can be found on page 81.

DEPARTMENT OF ECONOMIC AND COMMUNITY DEVELOPMENT

(15) Office of Community Development

Community Development Block Grant
CFDA # 14.228 Questioned Costs: $649,545

Finding: Release of grant funds without environmental review clearance request or approval

The Department of Economic and Community Development (DECD) released $649,545 to a municipality prior to an environmental review. Title 24 CFR 58.22 and 58.71 states, in part, that a State may not commit Housing and Urban Development assistance funds until an Environmental Review Clearance has been obtained.

Recommendation:

We recommend that DECD not release Housing and Urban Development assistance funds to any subrecipient that has not received an Environmental Review Clearance approval.

Auditee Response:

DECD acknowledges this as an administrative failure but believes it represents an extremely rare occurrence. The department did its own internal review of 62 projects from FY 96 and found no similar errors. In the case identified by the Department of Audit, no issues of environmental concern ever arose. The complete environmental review record would have considered the project Categorically Excluded, Converted to Exempt.

(16) Office of Community Development

Community Development Block Grant
CFDA # 14.228 Questioned Costs: $308,204

Finding: Grant administrative procedures need to be strengthened (Prior Year Finding)

Of the 25 projects that were reviewed, there was insufficient documentation in the program files to support that:

- national objectives (24 CFR 570.200) were being met; (2 projects - $308,204)
- a budget had been prepared; (2 projects)
- required program data had been collected; and (3 projects)
- an environmental review had been performed. (1 project)

In one case, the Department of Economic and Community Development (DECD) approved a project requiring Housing and Urban Development (HUD) funds before HUD approval was received.

Recommendation:

We recommend that DECD only fund projects that meet national objectives of Title I of the Housing and Community Development Act of 1974. In addition, grant administration procedures should be strengthened in the areas of case file documentation and approval procedures.

Auditee Response:

This finding relates to three CDBG "Regional Assistance Fund" (RAF) projects. In all three cases DECD differs with the Department of Audit on the question of the projects meeting the national objectives of the CDBG program and conducting CDBG eligible activities. The department believes the projects both meet national objectives and are being used for eligible activities. DECD understands that required program data should be collected.

DEPARTMENT OF ECONOMIC AND COMMUNITY DEVELOPMENT

In accordance with the Department of Audit's recommendation, DECD will carefully scrutinize all current RAF projects to ensure they meet all program requirements. Monitoring procedures will be applied to ensure compliance.

DEPARTMENT OF EDUCATION

(17) Bureau of Vocational Rehabilitation Services

Rehabilitation Services Basic Support
CFDA# 84.126 Questioned Costs: $50,339

Finding: Inadequate support for salary charged to grant

The State Accessibility Coordinator is responsible for reviewing State facilities for compliance with handicapped accessibility laws. There is no indication that this activity is directly related to the primary objective of this program, which is to provide services necessary to render employable an individual with handicaps. Therefore, we question the costs of the salary of the State Accessibility Coordinator charged to the program.

Recommendation:

We recommend that the Department of Education not charge the costs for the State Accessibility Coordinator to the Rehabilitative Services Basic Grant.

Auditee Response:

The Bureau of Vocational Rehabilitation Services was transferred from the Department of Education to the Department of Labor, effective for fiscal year 1997. Corrective action to resolve this finding will be implemented by the Department of Labor.

(18) Bureau of Vocational Rehabilitation Services

Rehabilitation Services Basic Support
CFDA# 84.126 Questioned Cost: None

Finding: Inadequate payroll records

Office of Management and Budget (OMB) Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments,* states:

> Where employees are expected to work solely on a single federal award, charges for their salaries must be supported by periodic certifications prepared at least semi-annually. These certifications may be signed by the employee or supervisory official having knowledge of the work performed by the employee. Where employees work on multiple federal grants or cost objectives the personnel activity reports must meet the following standards:
>
> 1. they must reflect an after the fact distribution of the actual activity of each employee,
> 2. they must account for the total activity for which each employee is compensated,
> 3. they must be prepared at least monthly and must coincide with one or more pay periods, and
> 4. they must be signed by the employee.

The Bureau of Vocational Rehabilitation Services (VRS) does not maintain payroll records that identify time spent on the Federal program. VRS does not prepare periodic certifications as required.

Recommendation:

We recommend that VRS maintain the required records.

Auditee Response:

. . .Upon moving to the Department of Labor the Bureau began using the approved allocation methodology.

(19) Workforce Education Team
Division of Applied Technology

Vocational Education - Basic Grants to States
CFDA# 84.048 Questioned Costs: None

Finding: Inaccurate and untimely filing of State annual financial reports

Per 34 CFR 80.41, the State is required to file annual (SF 269) financial reports for all grants 90 days after the end of the grant year. The SF 269 that was due on December 29, 1996, was not filed until May 2, 1997. Also, there were errors in line items and in the total amount of expenditures reported on the 1993 grant final report.

Recommendation:

We recommend that finance personnel and program administrators review and approve the financial reports for accuracy and timeliness.

The Department should file an amended SF 269 for the 1993 grant.

Auditee Response:

The accounting supervisor within the Finance Sub-Team will now be responsible for reviewing the SF 269 reports for all grants. The reviews will include the involvement of each Team Leader and/or their designee. The Finance Sub-Team will file an amended SF 269 report for the 1993 Carl Perkins - Vocational Education grant by the end of August, 1997.

(20) Workforce Education Team
Division of Applied Technology

Vocational Education - Basic Grants to States
CFDA# 84.048 Questioned Costs: None

Finding: No monitoring or testing for maintenance of effort (Prior Year Finding)

A maintenance of effort requirement is established by 34 CFR 403.182. Although the requirement was satisfied, neither the program administrators nor the finance division monitors compliance.

Recommendation:

Departmental personnel should test for maintenance of effort on an ongoing basis during the fiscal year.

Auditee Response:

The Workforce Education Team will continue to monitor the allotment of maintenance of effort and will forward the documentation to Finance for reporting purposes.

(21) Workforce Education Team
Division of Applied Technology

Vocational Education - Basic Grants to States
CFDA# 84.048 Questioned Costs: None

<u>Finding</u>: Subgrantee annual financial reports submitted after deadline (Prior Year Finding)

Subgrantees must conform with *Uniform Guidelines for Local Applications for Assistance to Eligible Recipients Under Titles II(B) & III(A) of the Carl D. Perkins Vocational and Applied Technology Education Act of 1990 (P.L. 101-392).* These guidelines require them to submit year-end annual financial reports by August 1 of each grant year.

For the year ended June 30, 1996, 19 of the 27 subgrantees filed their annual financial reports late. The reports, which on average were 77 days late, represented $1,483,183, or 41% of the total grant award to subgrantees.

<u>Recommendation</u>:

Program administrators should make every effort to receive timely reports from subgrantees.

<u>Auditee Response</u>:

The Department recognizes late reporting as an ongoing problem and when the finding was first reported, the Workforce Education Team (formerly Division of Applied Technology) did implement a system for flagging subrecipient noncompliance. Sanctions were imposed to withhold grant payments and grant awards until all reports were submitted. At no time are payments allowed to continue if the subrecipient has not complied with the reporting requirements of the grant.

The Department has implemented procedures and imposed sanctions but it cannot file the report for the subrecipient nor can it provide courier service to bring the report to the Department. Further, we believe it would not be in the best interest of local education to indefinitely withhold payments or grant awards or continue to penalize the subrecipient after the report(s) has been filed.

(22) Workforce Education Team
Division of Applied Technology
Division of Special Services

Vocational Education - Basic Grants to States
Special Education - Grants to States
<u>CFDA#</u> 84.048/84.027 <u>Questioned Costs</u>: None

<u>Finding</u>: Lack of approval on grant payment requests

Payments to subrecipients are submitted to the Finance Division of the Department of Education on the Grant Accounting System Recipient Award Form with no indication of authorization or approval from the program administrators. Other payment requests are submitted on a form letter from the Commissioner of Education, again, without any indication of approval by grant administrators. Program administrators should approve payments to be charged against the grant to ensure the allowability of expenditures under Federal regulations.

Recommendation:

Payments of grant funds should be made only if accompanied by documents authorized and approved by a grant administrator.

Auditee Response:

. . .an authorized official from the Workforce Education Team will approve the Grant Accounting System Recipient Award form before it is forwarded to Finance for payment. Manifests will also receive authorized approval from a grant administrator prior to payment.

(23) Workforce Education Team
Division of Applied Technology

Vocational Education - Basic Grants to States
CFDA # 84.048 Questioned Costs: $70,184

Finding: Inadequate support for salary charged to grants

Per Office of Management and Budget (OMB) A-87, *Cost Principles for State, Local and Indian Tribal Governments*, "where employees work on multiple activities. . . a distribution of their salaries. . . will be supported by personnel activity reports or equivalent documentation."

Although the Director's salary is entirely charged to this program, the position has responsibilities for other State and Federal programs.

Recommendation:

We recommend that the Director record time worked on each activity and charge that time accordingly.

Auditee Response:

We do not agree with the auditor's finding. The Carl D. Perkins Vocational and Applied Technology Education Act (CDPVATEA) is the primary source of Federal assistance to States and localities for workforce and technical education. The School-To-Work Opportunities Act (STWOA) is the other major source of Federal support for workforce education. It is entirely complementary to the Perkins Act, not a competing initiative.

Since we do not differentiate between CDPVATEA activities and STWOA activities, allocating the Director's time between the two would be a meaningless exercise. Further, the Department has contacted the U.S. Department of Education, Office of Vocational and Adult Education to obtain written approval that the allocation of 100% of the Director's salary to the Carl D. Perkins Act in fiscal year 1992 was then and is now an appropriate charge to the grant.

(24) Division of General Rehabilitation Services

Vocational Rehabilitation
Basic Support Program
CFDA# 84.126 Questioned Costs: None

Finding: Case file documents missing

Of the 65 case records reviewed, there was insufficient documentation in 9 case files to comply with Federal regulations (34 CFR 361). The following documents were missing:

Confidentiality statement	1 case
Comparable services available	1 case
Signed application	2 cases
Written notice of case closure	2 cases
Notice of appeal rights at closure	3 cases

Recommendation:

We recommend that the Department of Education retain all required documentation.

Auditee Response:

Department of Education

The Bureau of Vocational Rehabilitation Services was transferred from the Department of Education to the Department of Labor, effective for fiscal year 1997. Corrective action to resolve this finding will be implemented by the Department of Labor.

Department of Labor

The Division of Vocational Rehabilitation has recently implemented a new accountability system which we believe will effectively address casework documentation requirements. Our casework supervisor work group is now utilizing a new process to assure statwide consistency in meeting Federal requirements. We will address the issues raised in your findings with this group and increase staff understanding of these requirements through the training we are doing is each office on a monthly basis. Compliance will be monitored through peer, supervisory and managerial case reviews as we prepare for the FFY 98 RSAS Comprehensive Review.

(25) Division of Special Services

Special Education - Grants to States
CFDA # 84.027 Questioned Costs: $122,000

Finding: Inadequate support for salaries charged to grant

Per Office of Management and Budget (OMB) Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments*, "where employees work on multiple activities. . . a distribution of their salaries. . .will be supported by personnel activity reports or equivalent documentation." It also states that "budget estimates or other distribution percentages determined before the services are performed do not qualify as support for charges to federal awards."

The salaries for the Director and the Program Leader, are charged to this grant. At the end of each month, 10% and 5%, respectively, are then allocated to another program. We could not locate a time study or any other basis for this allocation; therefore, we question the salaries.

Recommendation:

We recommend that the Director and Program Leader allocate and record their time based on actual hours worked.

Auditee Response:

The Team Leader and Program Team Leader will record their time on the "Weekly Attendance & Time Distribution Report" (implemented by the Department in January, 1995) based on actual hours worked for the Technology Related Assistance to Individuals With Disabilities program and other programs involved.

(26) Office of Compensatory Education

Title I Grants to Local Educational Agencies
CFDA # 84.010 Questioned Costs: None

DEPARTMENT OF EDUCATION

Finding: Financial reports not submitted timely

The State is required to establish report due dates (34 CFR 80.20). Of the 125 financial reports reviewed, 72 reports (58%) were submitted after the deadline established by the Department of Education (DOE). These reports, which were prepared by Local Educational Agencies included:

	Late Reports	Average Number of Days Late
• Annual financial reports	21	58
• Annual performance reports	21	58
• Carryover request reports	8	64
• Consolidated application for funds reports	22	68

Recommendation:

DOE should make every effort to receive the required reports on time.

Auditee Response:

The Department does maintain procedures to monitor subrecipient reporting in accordance with federal regulations. It is the subrecipient's responsibility to comply with those regulations. Pre-award notifications and required reports are mailed to subrecipients in mid-May. The due date for each report is clearly marked on the front page. In addition, the due dates for ALL reports are listed in the Department's Administrative Calendar developed by the Department for LEA reporting.

Payments to subrecipients are not made until all prior year's financial and demographic data is received as well as receipt and approval of the current year's application. This information is maintained via the IASA Log Sheet Tracking System. On a monthly basis, this log is used to determine if LEA has filed the appropriate paperwork and is eligible to receive funds. If the LEA is eligible to receive funds, the Finance Sub-Team is notified to release payments to the subrecipient. At no time are payments allowed to continue if the subrecipient has not complied with the reporting requirements of the grant.

During the program year, the Office of Compensatory Education periodically contacts LEA's to follow up on any outstanding paperwork.

Because the Office of Compensatory Education has implemented procedures, does impose sanctions when the requirements are not met, and continues to monitor noncompliance with the reporting requirements of the grant, we believe this ongoing finding of late should be audited by the LEA auditor and corrective action addressed at the local level.

DEPARTMENT OF EDUCATION

(27) Office of Compensatory Education

Title I Grants to Local Educational Agencies
CFDA # 84.010 Questioned Costs: None

Finding: Local Educational Agencies not monitored

Title 34 CFR 200.43 (f)(1) states that the "SEA (State Educational Agency) shall monitor Local Educational Agencies (LEA's) compliance with the comparability requirements." For receipt of Title I funds, the LEA's, on a districtwide basis, use State and local funds to provide services in project areas that, taken as a whole, are at least comparable to services being provided in school attendance areas that are not receiving funds.

Title 34 CFR 200.44 requires that an LEA may only use funds to supplement (not supplant) non-Federal funds. The LEA's should increase the level of nonfederal funds that would, in the absence of the Federal funds, be made available for the education of pupils participating in Title I projects.

The Department of Education (DOE) failed to monitor the LEA's and therefore did not determine compliance with these requirements.

Recommendation:

We recommend that DOE monitor the LEA's for compliance with Federal and State regulations.

Auditee Response:

LEA's were not monitored during this audit period because time was needed to implement new regulations and develop a consolidated monitoring process with all IASA programs. Division personnel implemented the consolidated monitoring process during FY 97 and visited over 50 sites. A schedule has been developed to review each LEA throughout fiscal year 2000. The schedule has been published in the Mainely IASA newsletter. Multiple copies of the newsletter were mailed to each local IASA contact person for distribution throughout their area.

EXECUTIVE DEPARTMENT

(28) Maine Office of Substance Abuse

Substance Abuse Prevention and
Treatment Block Grant
CFDA# 93.959 Questioned Costs: $114,553

Finding: Failure to obligate and expend funds in proper periods

The Maine Office of Substance Abuse (MOSA) obligated $2,700 for subrecipient contracts against the Federal fiscal year 1994 Substance Abuse and Treatment Block Grant after the close of the first fiscal year of the grant, in violation of 42 USC 300 x-62.

In addition, $114,553 was expended after the end of the succeeding fiscal year, also in violation of regulations.

Recommendation:

We recommend that MOSA obligate and expend funds within the time allowed.

Auditee Response:

There were a number of contributing factors responsible for this audit finding. Those factors include the following:

- *A loss of State General funds and staffs as a result of State down sizing including the Office of Fiscal Manager. With the loss of State General funds ($875,000 in SFY 96 and $1,000,000 in SFY 97). the major priority for the Office was to reprioritize planned expenditures and implement new subrecipient contracts.*
- *During this Federal Block Grant period, the State was required to implement new set-aside requirements. In order to do so, the Office of Substance Abuse was required by new State Legislation to comply with a Request for Proposal (RFP) procedure. This RFP process delayed implementation of set-aside requirements and as a result, delayed the obligation and expenditure of Federal Fiscal Year 1995 funds.*
- *Due to the Request for Proposal State requirement, new programs were selected to deliver services. As new programs, they experienced startup difficulties and thus expenditure of funds was delayed.*

In late calendar year 1996, a new director was appointed to oversee the Office of Substance Abuse. In addition, the Office was reorganized in early calendar year 1997. A major priority of the new director was the inclusion of a fiscal division. This division over the last seven months has been immersed in reconciling accounts, assuring compliance with State and Federal mandates, and establishing procedures and internal controls to tract and monitor obligations, set-asides, and expenditures. During the current state fiscal year (1998), this division will implement two new systems designed to track contracts internally and all grant obligations, expenditures, and income based upon the state fiscal year and the corresponding federal fiscal year. This will enable the Office to monitor activity in a much more accurate and accessible manner. The systems will also enable us to detect potential issues will in advance and allow *sufficient time for corrective action. We expect that within twelve (12) to twenty-four (24) months all grant and contract activity will be monitored in this manner.*

Also, planning for new Federal obligations (FFY 1997) and the implementation of these obligations is well ahead of schedule compared to the previous fiscal year. For the next fiscal period (FFY 1998), it is the intent of the director to have the planning process for obligations completed by the end of the third quarter of the State fiscal year (FY 1998). By planning a quarter in advance, it is expected that all federal funds will be obligated thus ensuring compliance with both the obligations and the expenditure requirement. In addition to advance planning, all contract cycles will be changed to an "on cycle" schedule (7/1/ - 6/30) to coincide with the SFY and allow use of state accounting systems for accurate tracking and documentation.

(29) Maine Office of Substance Abuse

Substance Abuse Prevention and
Treatment Block Grant
CFDA# 93.959 Questioned Costs: $1,588

Finding: Duplicate payments made/Returned check not deposited

We tested 25 transactions and identified duplicate payments of $1,568, and a returned check for $20 that was not deposited until after the end of the grant year.

Recommendation:

We recommend that MOSA seek reimbursement for the identified overpayments, and that MOSA consult with the Federal grantor for the disposition of any proceeds received.

We also recommend that MOSA consult with the Federal grantor to determine the proper disposition of the proceeds from the $20 returned check.

Auditee Response:

$20.00 returned check for Alcohol Prevention Support Services:

Upon detection, this check was immediately deposited as a refund against the original expenditure. Internal controls and the Office of Substance Abuse Fiscal Policies and Procedures Manual will be reviewed and updated to address this issue. This will ensure that all returned checks will be deposited within three (3) business days. In addition, any checks received and not deposited the same day, will be kept under lock and key until ready for deposit. Since these funds were from our FFY 1995 grant, which expired in September 1996, we will consult with the *federal grantor to determine the proper disposition of these funds. After receiving instructions from our grantor, we will make the necessary accounting adjustments relating to this specific deposit as instructed (i.e. return funds or reexpend on similar functions).*

$1,568.00 overpayments for airline tickets:

Upon detection of this error, our accounts payable clerk has been instructed to review our airline payment records for discrepancies. Upon completion of this review, we will make the necessary accounting adjustments relating to these changes in order to ensure that the appropriate account(s) have been charged. We will also request a refund for any overpayment and apply these funds as a refund against the original funding source(s). Since these funds were from our FFY 1995 grant, which expired in September 1996, we will consult with the federal grantor to determine the proper disposition of these funds and make the necessary accounting adjustments relating to this specific deposit as instructed (i.e. return funds or reexpended on similar functions). Internal controls and the Office of Substance Abuse Fiscal Policies and Procedures Manual will be reviewed and updated to address this issue. This will ensure that all future payments are made against current activity only, and that any statement balances will be researched to determine status of payment. In addition, credits for canceled or returned tickets will be coded as refunds against the original funding source.

(30) Maine Office of Substance Abuse

Substance Abuse Prevention and
Treatment Block Grant
CFDA# 93.959 Questioned Costs: $77

Finding: Purchased airline services not used

The Maine Office of Substance Abuse (MOSA) purchases "no refund" airline tickets at lower prices than full fare.

MOSA is now holding unused airline tickets which cost a total of $547. Of this amount, $77 was charged to the Substance Abuse Prevention and Treatment Block Grant; the source of funds for the remaining $470 is unknown.

Recommendation:

We recommend that MOSA only charge the grant for goods or services received or used.

Auditee Response:

As indicated for the prior finding, upon detection of this error, our accounts payable clerk has been instructed to review our airline payment records for discrepancies. Upon completion of this review, we will make the necessary accounting adjustments relating to these charges in order to ensure that the appropriate account(s) have been charged. Any unused tickets will be canceled and a request for refund or credit will be sent to the vendor. Any refund or credit will be applied against the original funding source(s). Since these funds were from our FFY 1995 grant, which expired in September 1996, we will consult with the federal grantor to determine the proper disposition of these funds and make the necessary accounting adjustments relating to this specific deposit as instructed (i.e. return funds or reexpend on similar functions). Internal controls and the Office of Substance Abuse Fiscal Policies and Procedures Manual will be reviewed and updated to address this issue. This will ensure that any future unused airline tickets are immediately returned for credit or refund and that these adjustments are applied against the original funding source(s).

(31) Maine Office of Substance Abuse

Substance Abuse Prevention and
Treatment Block Grant
CFDA# 93.959 Questioned Costs: $689

Finding: Incorrect handling of refund

A subrecipient refunded $689 to the Maine Office of Substance Abuse (MOSA) after the end of the Federal grant year.

MOSA did not return the refund to the Federal grantor, but credited it to the closed grant.

Recommendation:

We recommend that MOSA consult with the Federal grantor regarding grant reimbursements.

Auditee Response:

*Upon receipt, this check was immediately deposited as a refund against the original expenditure. Since these funds were from our FFY 1993 grant, which expired in September 1994, we will consult with the federal grantor to determine the proper disposition of these returned funds. After receiving instructions from our grantor, we will make the necessary accounting adjustments relating to this specific deposit as instructed (i.e. return funds or reexpended on similar function(s)***.**

(32) Maine Office of Substance Abuse

Substance Abuse Prevention and
Treatment Block Grant
CFDA# 93.959 Questioned Costs: None

Finding: Independent peer review of service providers not performed (Prior Year Finding)

Title 42 USC 300x-53 requires that an independent peer review of service providers be conducted every year that the grant is provided. The Maine Office of Substance Abuse (MOSA) did not obtain an independent peer review of service providers for fiscal year 1996.

Recommendation:

We recommend that MOSA obtain independent peer reviews of service providers for each year that the grant is provided, and document that the review was conducted in accordance with grant regulations.

Auditee Response:

The Office of Substance Abuse will submit a technical assistance request no later than August 1997. The Office will assemble a group of community providers to begin the peer review process prior to September 1, 1997. The group will include prevention as well as treatment providers.

(33) Maine Office of Substance Abuse

Substance Abuse Prevention and
Treatment Block Grant
CFDA# 93.959 Questioned Costs: None

Finding: Incomplete subrecipient data in FFY 96 block grant application

Title 42 USC 300x-52 requires the block grant application to include a report of the two previous years' activities, including a description of subrecipients.

Only three of eight subrecipients tested, who either had funds obligated to them or had expenditures made to them, could be found listed in the report.

Recommendation:

We recommend that the Maine Office of Substance Abuse use due care when recording subrecipient data in annual block grant applications in order to be in compliance with grant regulations.

Auditee Response:

Complying with the obligation requirement by planning in advance will reduce the likelihood of incomplete subrecipient data. However based on performance, OSA reserves the right to reduce funding, withholding payments, and even terminate subrecipient contracts. In the event of any variance in previously reported subrecipient data, the Office of Substance Abuse will through the Block Grant application provide corrections and/or revisions. In addition to performance review, all contract cycles will be changed to an "on cycle" schedule (7/1 - 6/30 to coincide with the SFY and allow use of state directors to attempt to change obligation and set-aside requirements in the Block Grant to allow states to be able to respond in a timely and creative way to a rapidly changing behavior health environment.

(34) Maine Office of Substance Abuse

Substance Abuse Prevention and
Treatment Block Grant
CFDA# 93.959 Questioned Costs: None

Finding: Failure to meet maintenance of effort requirement for State fiscal year 1996

Text of finding can be found on page 104.

(35) Maine Office of Substance Abuse

Substance Abuse Prevention and
Treatment Block Grant
CFDA# 93.959 Questioned Cots: None

Finding: Grant management procedures are not sufficient to ensure compliance with expenditure requirements

Text of finding can be found on page 105.

DEPARTMENT OF HUMAN SERVICES

(36) Bureau of Child and Family Services

Foster Care - Title IV-E
CFDA # 93.658 Questioned Costs: $125

Finding: Eligibility compliance requirement not met

One $125 payment, of twenty-five disbursements totaling $4,235, should not have been charged to Federal funds because the provider was not licensed by the Department of Human Services (DHS) as required by 42 USC 671(a)(10) and 672(c).

Recommendation:

We recommend that DHS use due care to ensure that only allowable charges are made to Federal funds.

Auditee Response:

We agree with the audit finding and the recommendation. The provider was at one time licensed by the Department. However, at the time of the service in question the Provider no longer had a valid license.

(37) Bureau of Child and Family Services
Division of Purchased and Support Services

Social Services Block Grant
CFDA # 93.667 Questioned Costs: None

Finding: Variances in annual utilization report (Prior Year Finding)

Title 42 USC 1397 (e) requires annual activity reports that include service data and expenditures for the Social Services Block Grant. We noted several errors in the Federal fiscal year 1995 utilization report, submitted by the Department of Human Services (DHS).

Amounts reported by the Department of Mental Health and Mental Retardation, by the Department of the Attorney General and by DHS Day Care did not agree with the State Controller's monthly expenditure reports. Expenditures on the utilization report were understated by $437,288 (a variance of 3.4%).

Recommendation:

We recommend that DHS review the computation of expenditure amounts as well as coordinate information with other departments and review the reports for accuracy. We also recommend that DHS file a revised 1995 report, and maintain documents to support the revisions.

Auditee Response:

. . .DHS will be requesting expenditure information from the Attorney General's Office and the Department of Mental Health and Mental Retardation quarterly. . ..

(38) Bureau of Family Independence

Food Stamps
CFDA # 10.551 Questioned Costs: None

Finding: Absence of detail for outstanding claims (Prior Year Finding)

Each State agency is required to maintain an accounting system that, at a minimum, is designed to readily identify households that owe outstanding payments on claims (7 CFR 273.18 k).

The Bureau of Family Independence (BFI) does not maintain a detailed list of individuals and associated outstanding claims due to the State. Instead, the information is aggregated from the regional offices and computed each quarter for the FNS-209 Financial Status Report. At June 30, 1996, the amount reported on the FNS-209 Financial Status Report was $3,535,502. Because a detailed list is neither maintained nor readily available through the WELFRE computer system, BFI cannot readily identify households that have outstanding claims due.

Recommendation:

We recommend that BFI improve the computer program in order to provide a detail of the amount reported on the FNS-209 Financial Status Report.

Auditee Response:

. . .DHS' Division of Technology Services is working on this problem. . ..

(39) Bureau of Family Independence

Food Stamps
CFDA # 10.551 Questioned Costs: None

Finding: Collection summary for Financial Status Report not reconciled (Prior Year Finding)

According to 7 CFR 273.18 (k):

> Each State Agency shall be responsible for maintaining an accounting system for monitoring claims against households. At a minimum, the accounting system shall be designed to readily. . . . Document the circumstances which resulted in a claim, the methods used to collect the claim. . . . Document how much money was collected in payment of a claim and how much was submitted to FNS.

The Bureau of Family Independence (BFI) maintains a computerized system to record food stamp overpayments received during the quarter. This information is then reported on the Financial Status Report (FNS-209). The Fraud, Investigation, and Recovery Unit's records (Statistical Report) reflected $3,000 more than was reported in the FNS-209.

Recommendation:

To ensure accurate reporting of overpayments collected, we recommend that BFI reconcile the record of food stamp overpayments received and the amount reported on the FNS - 209 Financial Status Report. If the information on the FNS-209 is incorrect, we recommend that BFI repay $3,000 to the Federal government.

Auditee Response:

The two FNS reports. . .won't match and are used for different purposes.

(40) Bureau of Family Independence

Aid to Families with Dependent Children
CFDA # 93.560 Questioned Costs: None

Finding: Noncompliance with quality control transmittal requirements (Prior Year Finding)

The Department of Human Services (DHS) is required to dispose of, and submit, all case samples within 120 calendar days of the end of the month (45 CFR 205.42).

Of the 25 cases reviewed, 8 cases had not been submitted to the U.S. Department of Health and Human Services within the proper time frame. These 8 cases were transmitted an average of 9 days late.

Recommendation:

We recommend that DHS report the results of the quality control reviews within the required time period.

Auditee Response:

The BFI will redouble its efforts. . .to assure that cases are prepared for transmittal. . . as outlined in 45 CFR 205.42(e)(I)(c). . ..

DEPARTMENT OF HUMAN SERVICES

(41) Bureau of Family Independence

Jobs Opportunities and Basic Skills Program
CFDA# 93.561 Questioned Costs: None

Finding: Federal reports submitted late

The Department of Human Services (DHS) is required to submit an Annual Target Group Expenditure Report (FSA-302) to the Family Support Administration 45 days after the end of the Federal fiscal year. The FSA-302 for Federal fiscal year 1996 was submitted 18 days after the due date. The Quarterly Report of IV-F Expenditures (FSA-332) is also due to the Family Support Administration 45 days after the close of each quarter. Two of the four FSA-332's for fiscal year 1996 were submitted late: one was submitted one day late and the other was submitted 59 days late.

Recommendation:

We recommend that DHS submit both the annual FSA-302 and the quarterly FSA-332 as required. We further recommend that the FSA-331, which is used to prepare these reports, be forwarded to the Bureau of Family Independence on its preparation date.

Auditee Response:

The Division of Financial Services will ensure in the future that the Bureau of Family Independence receives a copy of the FSA-331 to assist BFI in preparing their FSA-302 and FSA-332 in a timely manner.

(42) Bureau of Family Independence

Jobs Opportunities and Basic Skills Program
CFDA# 93.561 Questioned Costs: None

Finding: Federal financial data incorrectly reported

The Department of Human Services (DHS) incorrectly reported expenditures on the Federal fiscal year 1996 Annual Target Group Expenditure Report (FSA-302), due to an incorrect calculation of the ratio of target group expenditures to total expenditures. As a result, Social Security Act, Title IV-F expenditures for target group individuals were overreported, while expenditures for non-target group individuals were underreported, by $55,619.

DHS also incorrectly reported expenditures on the quarterly report of IV-F expenditures (AFC 332). This was due to an incorrect calculation of the supportive services (program costs only). As a result, expenditures were underreported by $3,315.

Recommendation:

We recommend that DHS file amended reports. We further recommend that DHS review reports for accuracy before submission.

Auditee Response:

Corrected reports were prepared and submitted 7/18/97. In the future, ratio computation will be proofed by other than the preparer.

(43) Bureau of Family Independence

Job Opportunities and Basic Skills Program
CFDA# 93.561 Questioned Costs: None

Finding: Noncompliance with case record data requirements

The State must maintain an individual case record for each Job Opportunities and Basic Skills Program (JOBS) participant, to include assessment and employability development planning (45 CFR 250.82). The Department of Human Services (DHS) ASPIRE/JOBS Program Rules (Chapter 607) require the following:

1. Each AFDC recipient who is mandated to participate, or volunteers to participate in the JOBS program will complete a service application form. . . to determine the services required for the employment goal; and

2. ASPIRE/JOBS will contact participants by mail in order to schedule a initial appointment for an assessment. The letter will advise the participant that failure to appear for the appointment or contact the ASPIRE/JOBS office on or before the date of the appointment with good cause (as determined by ASPIRE/JOBS), or requesting conciliation, will result in notification being sent to the Bureau of Family Independence Eligibility Unit to apply a sanction.

Of ten case files examined, three did not contain a service application and three did not contain an Employability Development Plan.

Recommendation:

We recommend that DHS strengthen procedures to ensure that all data requirements are met related to case record information.

Auditee Response:

We concur that the deficiencies noted did occur. Steps have been taken to correct these deficiencies. . ...

(44) Bureau of Family Independence

Job Opportunities and Basic Skills Program
CFDA # 93.561 Questioned Costs: None

Finding: Participant incorrectly classified as exempt

Recipients of Aid to Families with Dependent Children (AFDC), who live in a subdivision covered by the Job Opportunity Basic Skills Program (JOBS), are required to participate in JOBS unless determined to be exempt (45 CFR 250.30 (a).

Twenty-five case files were tested to determine whether qualified AFDC recipients are participating in the JOBS program. One beneficiary was incorrectly classified as exempt from JOBS. According to the case record, there was no indication that the individual met any of the exemption criteria.

Recommendation:

We recommend that the Bureau of Family Independence comply with requirements regarding participation in the JOBS program.

Auditee Response:

. . .procedures have been refined allowing action to be taken in regards to noncompliance in a more timely fashion.

(45) Bureau of Family Independence
Division of Data Processing

Medical Assistance Program
CFDA # 93.778 Questioned Costs: None

Finding: Social Security numbers not verified (Prior Year Finding)

Verification of an applicant's Social Security number with the Social Security Administration (SSA) is a preliminary step in the eligibility determination process, which is required by 42 CFR 435.948.

A test of paid health insurance claims revealed that the Department of Human Services (DHS) did not verify the Social Security numbers for two of twenty-five applicants. There is no questioned cost because documentation from the SSA shows that the Social Security numbers in question were valid.

Recommendation:

We again recommend that DHS independently verify Social Security numbers for program applicants.

Auditee Response:

The finding is a national problem which the Social Security Administration is attempting to fix. The problem is created when two or more tapes are sent to the Social Security Administration for verification. If the Social Security Administration does not run the tapes in chronological order, or if the action is on the last tape, the information is not returned to the State. The Social Security Administration is looking at date stamping the tapes as they are received so that they are run chronologically.

(46) Bureau of Family Independence

Medical Assistance Program
CFDA# 93.778 Questioned Costs: None

Finding: Noncompliance with quality control requirements

Title 42 CFR 431(P) establishes State plan requirements for a Medicaid eligibility quality control program. The Department of Human Services (DHS) must submit to the Health Care Financing Administration (HCFA) sampling plans, error rate calculations and corrective action plans. DHS could not provide copies of reports submitted; consequently, compliance with quality control reporting requirements could not be determined.

Recommendation:

DHS should evidence compliance with reporting regulations by maintaining copies of reports submitted.

Auditee Response:

. . .an accountant for HCFA. . .will assist BFI in accomplishing the complex calculations. . ..

(47) Bureau of Health

Special Supplemental Food Program
Women, Infants and Children
CFDA# 10.557 Questioned Costs: $1,402

Finding: Failure to make indirect cost adjustment (Prior Year Finding)

The State is required to adjust costs to actual when a provisional indirect cost rate is used (Allowable Costs/Cost Principles of the *Compliance Supplement for Single Audits of State and Local Governments*). This is also required by the State and Local Rate Agreement between the State of Maine, Department of Human Services (DHS), and the U.S. Department of Health and Human Services, Division of Cost Allocation.

DHS failed to adjust the provisional rate used for program year 1994 to the final rate calculated for indirect costs. As a result, it overassessed the indirect costs for the program by $1,402.

Recommendation:

We recommend that DHS file an amended report to correct the amount charged to indirect cost.

Auditee Response:

The indirect cost adjustment for program year 1994 has been made and reported to the United States Department of Agriculture.

(48) Bureau of Medical Services

Medical Assistance Program
CFDA# 93.778 Questioned Costs: None

Finding: Disproportionate share hospital (DSH) payments may not be within limits established by Federal regulation

Section 13621 of the Omnibus Budget Reconciliation Act of 1993 (OBRA 93) established limits on State disproportionate share hospital (DSH) payments. These limits apply to each State's total DSH payments and to DSH payments made to individual hospitals.

These limits were effective for State fiscal years beginning on or after January 1, 1995 -- for Maine, the effective date was July 1, 1995 (SFY 1996).

The State of Maine's 1998-99 biennial budget (Chapter 24 Public Law 1997) modified the State's planned phase-out of the hospital assessment and the so-called "tax and match" plan (the assessment and DSH payments for acute care hospitals will still be terminated at the end of SFY 1998). Under the budget law, the State and the hospitals agreed to hospital-specific "match" payments (i.e., DSH payments plus the allowable costs of the tax) and payments for SFY 1996. Because of the complexity of the calculations required under the budget law, it is not clear if the DSH payments assumed in the agreed upon "match" payments are within the limits envisioned in OBRA 93. While the DSH payments are for the most part calculated in a manner consistent with OBRA 1993, it appears that a net payable of $2,279,133 in SFY 1996 payments -- with the Federal share of this difference equal to $1,443,147 -- may not be in strict compliance with HCFA's interpretation of OBRA 1993. While not exceeding the overall DSH ceiling established by OBRA 1993, these payments may not be in strict compliance with the hospital specific limits. Because the final cost settlement process based on Medicare audited cost reports has not been completed, final payments to hospital's for SFY 1996, and therefore any payments that might be in excess of OBRA 1993 limits, cannot be definitively determined at this time.

Recommendation:

We recommend that the Department of Human Services (DHS) have additional discussions with the Health Care Financing Administration (HCFA) to ascertain whether DHS's interpretation of the DSH limit provisions in OBRA 1993 do in fact comply with HCFA's interpretation of the statute.

Auditee Response:

DHS believes both its preliminary and final calculation of DSH payments for SFY 1996 are/will be consistent with OBRA 1993 and will be allowed under HCFA's interpretation of the provisions of OBRA 1993.

(49) Bureau of Medical Services

Medical Assistance Program
CFDA # 93.778 — Questioned Costs: None

Finding: Noncompliance with Medicaid waiver approvals

During fiscal year 1996, the Department of Human Services (DHS) had four Medicaid waivers in effect to provide community and home-based services. The waivers are based upon an agreement with the Health Care Financing Administration (HCFA) to provide services for an estimated number of individuals at an estimated average amount per capita.

HCFA requires notification if, at any time during the waiver period, the actual number of individuals to be served or the average per capita expenditures exceed the estimates. DHS exceeded the approved number of individuals in two of the four waivers and the approved per capita estimated expenditures in three of the four waivers. HCFA was not notified until submission of the annual report.

Recommendation:

DHS should monitor data and notify HCFA as required.

Auditee Response:

The Department disagrees with this finding. . ..

(50) Bureau of Medical Services

Medical Assistance Program
CFDA # 93.778 Questioned Costs: None

Finding: Late filing of annual reports for Medicaid waiver programs

During fiscal year 1996, the Department of Human Services (DHS) had four Medicaid waivers to provide community and home-based services. An "Annual Report on Home and Community-Based Services Waiver" report (HCFA-372) is required to be submitted to the Health Care Financing Authority for each of the four waivers. The reports due in December, 1996, were not submitted until March, 1997.

Recommendation:

DHS should submit timely annual reports to ensure compliance with Federal reporting requirements.

Auditee Response:

The Department recognizes the 1996 report was not submitted in a timely fashion. The Department has taken steps to ensure timely submission of this report in the future.

(51) Bureau of Medical Services
Division of Financial Services

Medical Assistance Program
CFDA# 93.778 Questioned Cost: None

Finding: Incorrect accounting for suspense payments/Lack of monitoring of refunds for compliance with Cash Management Improvement Act

Section 10.3 of the Cash Management Agreement between the State and the U.S. Department of Treasury states, "Each State agency shall manually track and document refunds, which shall be offset against subsequent drawdowns of Federal funds. . .." Title 42 CFR 433.312(A)(2) states, "The agency must refund the Federal share of overpayments at the end of the 60 day period following discovery."

The Department of Human Services (DHS) credits refunds received against General Fund expenditures. Although DHS refers to this as "suspense," it is not a balance sheet account. Once DHS claims adjusters determine the final disposition of the amounts refunded, they enter the information into the Medical Management Information System. DHS then prepares a monthly journal to appropriately distribute the identified payments between State and Federal funds. In fiscal year 1996, $12 million was credited back to Federal expenditures from the Suspense account. Because there is a delay between refund receipt and credit to the Federal account, an interest liability may result. The process also creates General Fund allotment, which enables DHS to expend funds without Legislative approval.

Division of Audit notifies the Division of Financial Services (DFS) of overpayments identified via audit cost settlements. Whether or not the overpayments have been recovered, to comply with regulations, DFS reduces the next Federal drawdown. DFS also prepares a journal to establish a receivable and to transfer cash to the Federal fund from the General Fund. When refunds are received, DHS applies them against the General Fund receivable.

DHS does not manually track and document refunds as required. Because DHS has 60 days to remit refunds, DHS may be transferring funds from the General Fund sooner than is necessary.

Recommendation:

We recommend that DHS track and document refunds as required. DHS should also consider the timing of transfers from the General Fund. To ensure accurate financial statements and budgetary control over the funds recovered, we recommend that DHS account for unidentified refunds in a Suspense account on the balance sheet.

Auditee Response:

The DFS doesn't manually track individual Non-MMIS cycle transactions that are processed through the Medicaid accounts. With all the activity this would be a time consuming and burdensome task. On a weekly basis DFS adjusts the federal cash drawn based as the debits and credits that occurred in the Medicaid accounts during the previous week. It seems incredible that in finding #60 we are found not to be in compliance with the 60 days requirement for recording overpayments on the HCFA-64. But we are asked to hold off transferring overpayments until 60 days which could result in a delay in recording them on the HCFA-64 even longer. Under normal circumstance it takes around 45 days to transfer overpayments. It is unreasonable to ask DHS to hold on to these transactions until the last day.

(52) Bureau of Medical Services
Division of Licensing and Certification

Medical Assistance Program
CFDA # 93.778 — Questioned Costs: None

Finding: Noncompliance with health and safety survey regulations

1. The "State Plan Under Title XIX of the Social Security Act," Attachment 4.40C, states that Life Safety Code surveys conducted by the State Fire Marshal's Office are to be performed at the same time as, or within 12 days following, the health care surveys. Of 25 health and safety surveys tested, one provider's Life Safety Code survey was conducted two months after the health care survey.

2. "Survey, Certification and Enforcement Procedures" of 42 CFR 488 requires State survey agencies to use the survey methods, procedures and forms that are prescribed by the Health Care Financing Administration (HCFA). Of the 25 surveys tested, 4 were each missing one prescribed form from their survey packet. Of the 306 forms required, 302 were used.

3. HCFA Form 1539, "Medicare/Medicaid Certification and Transmittal," is the form used to transmit information to the Federal government regarding survey and certification actions. We noted that 10 of the 25 HCFA Forms 1539 had required fields left blank.

Recommendation:

1. In the event that an unavoidable delay occurs in completing a scheduled Life Safety Code survey, we recommend that written documentation of the facts of the situation be included in the survey packet.

2. We recommend that a supervisory review of completed surveys include determination that all forms required by HCFA to be used during the survey process have been utilized and properly completed, and are included in the survey packet.

3. In order to ensure that correct information is transmitted to the Health Care Financing Administration and entered into the OSCAR data base, we recommend that the surveyor complete all applicable fields on the HCFA 1539 transmittal report. We recommend that the supervisor review the form to ensure all applicable fields have been completed.

Auditee Response:

The Division of Licensing and Certification has a Memorandum of Understanding with the State Fire Marshal Office (SFMO) to have the SFMO provide Life Safety Code (LSC) reviews. The SFMO is notified of upcoming survey dates and schedules a LSC review within 12 days of the health care survey. The schedule is monitored and communication is effected with the SFMO if survey dates are not met.

In order to facilitate scheduling and conduct of LSC surveys, the Division of Licensing and Certification is in the process of linking the SFMO data base and the Division's scheduling data via FTP (File Transfer Protocol) software and expects to implement this by October 1, 1997. Inability to comply with established time limits will be documented, but is not a Federal requirement.

A procedure has been established whereby the State surveyor staff will be instructed to use all required HCFA survey forms during the survey process. Supervisors will be asked to ensure that all required forms are contained in the submitted survey packets and check the forms to ensure that the surveyors fill in all applicable fields on the HCFA 1539 Transmittal report.

(53) Bureau of Medical Services
Division of Licensing and Certification

Medical Assistance Program
CFDA # 93.778 Questioned Costs: None

Finding: Weak internal control over provider terminations (Prior Year Finding)

The Department of Human Services, Division of Licensing and Certification (Division) must terminate a facility's certification if it is determined that the facility no longer meets applicable requirements, or the facility's deficiencies pose immediate jeopardy to patients, health and safety (42 CFR 442.117 and .118).

The Division sends termination information to the Medicaid Management Information System's (MMIS) File Maintenance Unit, to have the provider removed from the claims processing system. We noted that the File Maintenance Unit was not informed of all terminations.

Recommendation:

To ensure that a terminated facility is removed from the provider payment system, we recommend that the Division of Licensing and Certification send a formal letter to the Director of the Data Resolution Unit and the team leader of the File Maintenance Unit, notifying them that a facility was terminated.

Auditee Response:

The Division of Licensing and Certification has now established procedures whereby a formal letter is sent to the Data Resolution Unit and the File Maintenance Unit of the Bureau of Medical Services notifying them when a provider or a facility is terminated from the provider/supplier payment system. Additionally, the Data Resolution Unit will receive a second notification of the same when the Division's Directories are updated or changed.

DEPARTMENT OF HUMAN SERVICES

(54) Disability Determination Services

Social Security - Disability Insurance
CFDA # 93.802 Questioned Costs: None

Finding: Expenditures incorrectly reported

Expenditures reported on the State Agency Report of Obligations (SSA-4513) for the quarter ended June 30, 1996, were understated by $4,851. This was due to the omission of allowable indirect costs for April, 1996.

Recommendation:

We recommend that Disability Determination Services reconcile expenditures on the SSA-4513 to quarterly expenditures on the State Controller's records to ensure the accuracy of data.

Auditee Response:

Disability Determination Services' procedures have been revised to include reconciling the year-to-date expenditures on the SSA-4513 to the Controller's B919 cash report.

(55) Disability Determination Services

Social Security - Disability Insurance
CFDA # 93.802 Questioned Costs: None

Finding: Federal share of departmental indirect cost not drawn down

As of the date of audit, the Department of Human Services - Disability Determination Services (DDS) had not prepared the journal vouchers charging the Social Security Disability Insurance (SSDI) for the indirect costs for the 1995 and 1996 fiscal years. As a result, the State did not receive Federal reimbursement earned. SSDI's share of departmental indirect costs for the 1995 and 1996 fiscal years totaled $441,453.

After being advised of the issue, DDS personnel prepared the required journal vouchers.

Recommendation:

We recommend that DDS personnel prepare, on a quarterly basis, the journal voucher necessary to transfer funds for departmental indirect costs.

Auditee Response:

Subsequent to preparing the quarterly SSA-4513, DDS personnel will prepare the indirect cost journal to transfer the funds to the departmental indirect cost pool.

(56) Disability Determination Services

Social Security - Disability Insurance
CFDA # 93.802 Questioned Costs: None

Finding: Federal financial reports not submitted on time

The Department of Human Services - Disability Determination Services (DDS) must submit Cost-Effective Measurement System (CEMS) reports according to required due dates. The following CEMS reports were late:

Reporting period	Due date	Days late
10/1/95 - 12/31/95	02/15/96	5
01/1/96 - 03/31/96	05/15/96	4

Recommendation:

We recommend that DDS submit the CEMS reports within the required time frame.

Auditee Response:

DDS personnel realize reports must be submitted within the required time frame; and every attempt will be made to submit these reports on a timely basis.

(57) Division of Financial Services

Job Opportunities and
Basic Skills Program
CFDA# 93.561 Questioned Costs: None

Finding: Federal reports submitted late

The Aid to Families with Dependent Children Quarterly Report of Expenditures for Title IV-A Payments under JOBS and Child Care Expenditures (ACF-231) is due 30 days after the end of each quarter. All of the four reports tested were submitted late.

Reporting Period	Due Date	Number of Days Late
09/30/95	10/30/95	22
12/31/95	01/30/96	7
03/31/96	04/30/96	1
06/30/96	07/30/96	7

Recommendation:

We recommend that the Department of Human Services submit the quarterly ACF-231 when due.

Auditee Response:

DHS concurs with the above audit finding regarding the tardiness of the JOBS report. DHS will make every effort to submit these reports in a timely manner in the future.

(58) Division of Financial Services

Child Support Enforcement
CFDA # 93.563 Questioned Costs: None

Finding: Child support collections not reconciled (Prior Year Finding)

The Department of Human Services (DHS) - Division of Financial Services - Cashier Section receives and processes child support collections on the New England Child Support Enforcement System (NECSES). NECSES generates the *Daily Receipts Record* showing the amount of child support collections recorded on the system. DHS does not reconcile the *Daily Receipts Record* to the amount of revenue recorded by the State Controller.

Insufficient control procedures for processing receipts could result in misappropriated funds.

Recommendation:

We recommend that DHS reconcile the amount of receipts recorded on NECSES to the amount of revenue recorded on the State Controller's records.

Auditee Response:

DHS concurs with the finding. DHS staff have established a system to reconcile the NECSES Daily Receipts Record to the controller's Cash Receipt Statement effective 7/1/97.

DEPARTMENT OF HUMAN SERVICES

(59) Division of Financial Services

Medical Assistance Program
CFDA# 93.778 — Questioned Costs: $114,582

Finding: Failure to make indirect cost adjustments

The State is required to adjust costs to actual when a provisional indirect cost rate is used (Allowable Costs/Cost Principle of the *Compliance Supplement for Single Audits of State and Local Governments*). This is also required by the State and Local Rate Agreement between the State of Maine, Department of Human Services (DHS), and the U. S. Department of Health Services Division of Cost Allocation.

DHS failed to adjust the provisional rate used for fiscal year 1994 to the final rate calculated for indirect costs for that period. The difference between application of the two rates is $114,582.

Recommendation:

We recommend that DHS make the necessary adjustments.

Auditee Response:

The agency agrees with the finding and will be taking corrective action on the June 30, 1997 Health Care Financing Administration (HCFA-64) Federal financial report.

(60) Division of Financial Services

Medical Assistance Program
CFDA# 93.778 — Questioned Costs: None

Finding: Federal share of cost/audit settlement recoveries not refunded timely (Prior Year Finding)

Title 42 CFR 433.320 states that "the agency must refund the federal share of overpayments that are subject to recovery to HCFA (Health Care Financing Administration) through a credit on its Quarterly Statement of Expenditures (Form HCFA-64). The federal share of overpayments subject to recovery must be credited on the Form HCFA-64 report submitted for the quarter in which the 60 day period following discovery."

We examined ten hospital cost/audit settlements where the hospitals had been overpaid and were subject to recovery. Out of ten hospitals with overpayments over $200,000, eight of the refunds were not made on the Form HCFA-64 for the quarter during which the 60 day period after discovery fell. The Federal share of these overpayments totaled $3,080,544. The refunds to HCFA were from three to six months late.

Recommendation:

We again recommend that DHS record overpayments on the HCFA-64 report according to the sixty-day requirement.

Auditee Response:

Every effort is made to conform to this sixty day requirement on overpayments. Since a shortage of funds and staffing in FY 95 put the DFS behind in processing overpayments through the suspense account journal. This will result in trying to process more overpayments in a future year and running into a possible shortage of funds.

(61) Division of Financial Services

Various Federal Programs
CFDA # Various — Questioned Costs: None

Finding: Periodic certification requirement not met

Office of Management and Budget Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments*, states:

> Where employees are expected to work solely on a single Federal award or cost objective, charges for their salaries and wages will be supported by periodic certifications that the employees solely on that program for the period covered by the certification. These certifications will be prepared at least semiannually and will be signed by the employee or supervisory official having first hand knowledge of the work performed by the employee.

The Department of Human Services (DHS) was not aware of the reporting requirement, which became effective in September, 1995. DHS time records did not indicate the program(s) worked on and did not include the required certification.

Although the certification requirement was not met, our testing of 25 employee records indicated that all employees worked for the programs to which they were charged.

Recommendation:

We recommend that DHS implement the required certifications. We also recommend that DHS remain current with revisions to all laws and regulations.

Auditee Response:

The Department is developing a mechanism to identify accounts on individual weekly time reports.

(62) Division of Financial Services

Various Federal Programs
CFDA # Various — Questioned Costs: None

Finding: Federal financial reports submitted late (Prior Year Finding)

The program regulations listed below specify dates by which Federal financial reports must be submitted. Of the 32 financial reports tested, 21 were submitted after the due date.

Program Name/CFDA#	Citation	Number of Reports Submitted Late	Average No. of Days Late
State Administrative Matching Grants For Food Stamp Program CFDA #10.561	7 CFR 277.11 (4)	4	25
Child and Adult Care Food Program CFDA #10.558	7 CFR 226.7 (d)	2	2
Child Support Enforcement CFDA #93.563	45 CFR 301.15(a) (1)	1	9
AFDC CFDA #93.020	45 CFR 201.5(a) (1)	4	12.5
Foster Care - Title IV-E CFDA #93.658	45 CFR 74.73	2	8.5
Medical Assistance Program CFDA #93.778	42 CFR 430.30(c) (1)	4	62.5

Job Opportunities and Basic Skills Training Program CFDA #93.561	45 CFR 201.5(a) (1)	4	4.7

Recommendation:

We recommend that the Department prepare and submit the required Federal financial reports by the date they are due.

Auditee Response:

The Department of Human Services agrees with the finding. Every effort is made to comply with this finding, including the use of new reports from the Controller's Budget Management System to expedite information gathering capabilities as well as the SmartSuite applications recently installed. The goal of the Department is to submit all reports on time all the time.

(63) Division of Maternal and Child Health

Special Supplemental Food Program
Women, Infants, Children
CFDA # 10.557 Questioned Costs: None

Finding: Federal financial reports submitted late (Prior Year Finding)

Five of twelve Federal financial reports (FNS-498) were submitted after the due date established by 7 CFR 246.25 (b)(1). They were issued from one to twenty-seven days late.

Recommendation:

We recommend that the Department of Human Services prepare and submit reports as required.

Auditee Response:

The WIC Program was unable to meet the prescribed time frame due to 2 staff vacancies in the financial component of the Program. This problem has been resolved.

(64) Division of Maternal & Child Health

Special Supplemental Food Program
Women, Infants, Children
CFDA # 10.557 Questioned Costs: None

Finding: Local agency not monitored

The Department of Human Services (DHS) is required to monitor each local agency at least biennially per 42 USC 1786 (21). Of the eleven agencies tested, one had not been reviewed since September 12, 1993.

Recommendation:

We recommend that DHS monitor all local agencies as required.

Auditee Response:

The WIC Program was unable to monitor this local agency due to two staff vacancies in the nutrition component of the program. Both nutrition coordinator positions were vacant for almost two years due to a lack of eligible and qualified candidates. Both positions have been filled since April and the monitoring is now being accomplished.

(65) Division of Support Enforcement and Recovery

Child Support Enforcement
CFDA # 93.563 Questioned Costs: None

Finding: Child support collections not properly distributed (Prior Year Finding)

Title 45 CFR 302.32 requires the State to distribute child support collections in a specified sequence. The New England Child Support Enforcement Services (NECSES) Manual specifies the distribution parameters for the State of Maine.

NECSES is the application system used by the Department of Human Services (DHS) - Division of Support Enforcement and Recovery (SER) to account for child support collections and to distribute funds. The Department of Administrative and Financial Services - Division of Data Processing (DDP) is responsible for maintaining the NECSES computerized system.

Out of twenty-five transactions tested for proper distribution, one disbursement ($12.24) was applied to State/Federal reimbursement, instead of being disbursed as an AFDC GAP payment. The error occurred because receipts classified as State arrearages for obligations of one type were held because the children's status type was different from the obligation type.

SER personnel stated that this error type has been corrected as a result of several modifications to the NECSES application program as required for NECSES certification, due by October 1, 1997 (45 CFR 307). Further, SER personnel stated that the following functions will require program changes to bring NECSES into compliance with certification standards:

- Daily distribution module
- OCSE reporting
- Case level Unreimbursed Assistance (URA) distribution
- Child support enforcement network (CSENET)

Recommendation:

We recommend that DHS and DDP review the NECSES program to ensure that the application system correctly disburses child support monies in accordance with specifications.

Auditee Response:

Corrections to the automated system have been made and the agency is now confident that all future child support collections will be disbursed in accordance with NECSES distribution parameters.

(66) Division of Surveillance and Utilization Review

Medical Assistance Program
CFDA # 93.778 Questioned Costs: None

Finding: Late refunds of the Federal share of Medicaid overpayments

Six of fifteen Medicaid overpayments identified during surveillance and utilization reviews were not refunded to the Federal government according to the due date required by 42 CFR 433.312. One overpayment of $8,641 was refunded one quarter late and the other five had not been refunded as of July, 1997. The five were excluded because they had been transferred to "closed" computer files, which resulted in the data not being displayed when needed. A review of all "closed" computer files indicated that a total of $27,934 is due for the Federal share of overpayments contained in the closed computer files.

Recommendation:

The Division of Surveillance Utilization Review (SURS) should ensure that all refunds of the Federal share of overpayments have been made before computer files are closed. SURS should refund amounts past due of $27,934 to the Federal government for the Federal share of Medicaid overpayments.

Auditee Response:

Amounts past due. . .have been refunded. . .. Mechanisms are now in place to prevent this from recurring in the future.

DEPARTMENT OF HUMAN SERVICES

(67) Bureau of Employment Services

Job Training Partnership Act
CFDA# 17.246/17.250 Questioned Costs: None

Finding: Reported program expenditure not reconciled with the State Controller's records

In accordance with the Office of Management and Budget Circular A-128, *Audits of State and Local Governments*, the State of Maine is required to prepare a Schedule of Federal Financial Assistance which reflects total Federal expenditures. The Bureau of Employment Services (BES) provided expenditure information for the Job Training Partnership Act based on quarterly reports furnished by subrecipients. BES did not reconcile these quarterly reports with expenditure information as reflected in the Controller's records and did not perform required subrecipient monitoring activities. The unreconciled amount at June 30, 1996 was $792,635, or 4.9% of reported program expenditures of $16,291,348.

Recommendation:

We recommend that BES reconcile reported expenditures with the State Controller's records to assure their accuracy. Adequate subrecipient monitoring will enable BES to identify necessary reconciling items.

Auditee Response:

The BES currently reconciles subrecipient grant expenditures to the State Controller's records at the time of grant close-out. In addition, the BES completes audit desk reviews of Subrecipient Audit Reports to analyze revenues and expenditures by grant fund to grant payments made by the Department of Labor.

The BES concurs that an annual reconciliation of the quarterly reports to the Controller's records should occur in the absence of subrecipient monitoring. The BES has planned to conduct subrecipient monitoring in this program year at which time a reconciliation of the prior year-ending quarterly reports to the State Controller's records will be conducted.

DEPARTMENT OF LABOR

(68) Bureau of Employment Services

Job Training Partnership Act
CFDA # 17.246/17.250 Questioned Costs: None

Finding: Inadequate documentation of policies and procedures

The *Financial Management Procedures* manual maintained by the Bureau of Employment Services (BES), and the *Operating Policy and Procedures* manual maintained by 12 County Service Delivery Area (SDA), are incomplete because they do not include award and contracting procedures, the use of spreadsheets and Federal report preparation procedures.

Title 20 CFR 627.425 specifies that "recipients and subrecipients shall ensure that their own financial systems. . .shall include information pertaining to subgrant and contract awards, and obligations" and are "sufficient to permit preparation of required reports."

Recommendation:

We recommend that BES and 12 County SDA document procedures pertaining to awards and contracts, Federal reporting and the use of spreadsheets. Policies and procedures should be updated as necessary.

Auditee Response:

The BES has always maintained a financial system sufficient to permit preparation of all required federal reports. It includes a variety of spreadsheets, contract logs, award documentation, and a contract review process.

Contracting procedures are included in the BES Financial Management Procedures Manual. Although some changes in the contract forms have been made, no changes in the actual procedures have been made. As this manual will no longer be used due to the consolidation of the accounting units at the department level, effective July 1, 1996, contracting procedures will be reviewed and included in either the existing Financial Management Systems (FMS) manual or a new internal procedures manual.

Instructions for use in preparing federal reports are documented, but have not been formally incorporated into a manual. This function is being transitioned to the Department's newly merged accounting unit.

(69) Bureau of Employment Services

Job Training Partnership Act
CFDA # 17.246/17.250 Questioned Costs**:** None

Finding: Noncompliance regarding audits of subrecipient service providers (Prior Year Finding)

Title 20 CFR 627.480 (d) requires the recipient to ensure that the subrecipient comply with applicable audit requirements, resolve all audit findings that affect the program and maintain an audit resolution file that documents the disposition of all findings. In fiscal year 1996, the Bureau of Employment Services (BES) completed no reviews of audits.

Recommendation:

We recommend that BES establish and follow desk review procedures to ensure compliance with subrecipient audit requirements. BES should include a reconciliation of funding provided to the subrecipient to reported revenues. BES should also review supplemental schedules required under Section .2(E) of the *Maine Uniform Accounting and Auditing Practices.*

Auditee Response:

The desk review checklist will be revised to include procedures to reconcile revenues and expenditures reported in the audited financial statements with BES records. The checklist will also be revised to include a review of the supplemental schedules required by Section .02 of MAAP.

(70) Bureau of Employment Services

Job Training Partnership Act
CFDA # 17.246/17.250 Questioned Costs: None

Finding: Cash management procedures conflict with Cash Management Improvement Act (Prior Year Finding)

The Bureau of Employment Services (BES) and 12 County Service Delivery Area (SDA) draw down Federal funds to pay for administrative costs of programs funded by the State's General Fund. The process temporarily overcharges Federal funds and triggers cash drawdowns. Although BES and SDA later distribute the administrative costs equitably to Federal and State Accounts, any Federal cash drawdown used for State purposes could result in the State owing interest to the Federal government under the Cash Management Improvement Act (CMIA).

Title 31 CFR 205.12(a) states the following requirement:

> A state will incur an interest liability to the federal government if federal funds are in a state account prior to the day the state pays out funds for program purposes. A state interest liability will accrue from the day federal funds are credited to a state account to the day the state pays out federal funds for program purposes.

Recommendation:

We recommend that BES drawdown funds in accordance with the CMIA agreement.

Auditee Response:

The entire drawdown procedure will be reviewed and modified as a result of the consolidation of the fiscal units.

(71) Bureau of Employment Services

Job Training Partnership Act
CFDA # 17.246/17.250 Questioned Costs: None

Finding: Inadequate review procedures for the cost allocations (Prior Year Finding)

Management personnel at 12 County SDA do not review cost allocations to ensure that there are no incorrect expenditure allocations reported to 12 County SDA's oversight agency via quarterly financial reports.

Recommendation:

We recommend that 12 County SDA properly document its financial accounting and reporting systems according to the requirements of 20 CFR 627.425 and the Common Rule. We further recommend that it develop and implement written procedures that require a review of the indirect cost allocation before reporting those expenditures to the oversight agency.

Auditee Response:

As of July 1, 1996, the 12 County SDA financial accounting system (including the indirect cost allocation) are not maintained by the Department of Labor's Office of Administrative Services which operates in accordance with all required Federal and State Regulations and requirements.

Specifically, the allocation of indirect cost for the 12 County SDA is accomplished through the use of the Department of Labor's Cost Allocation System, DOLLARS - a nationwide U.S. Department of Labor system, which resulted in the discontinuation of the spreadsheets discussed above.

All reports generated by the Department of Labor's Office of Administrative Services are reviewed by each bureau to ensure that data has been entered and posted correctly prior to the preparation of financial reports.

(72) Bureau of Employment Security

Job Training Partnership Act
CFDA # 17.246/17.250 Questioned Costs: None

DEPARTMENT OF LABOR

Finding: Subrecipients not monitored (Prior Year Finding)

The Bureau of Employment Services (BES) did not monitor two of the three Service Delivery Area (SDA) providers as required by 20 CFR 627.475.

Recommendation:

We recommend that the BES monitor all SDA's as required.

Auditee Response:

The BES and Job Service Administration units merged in the spring of 1996 in an attempt to prepare for one-stop programming. The expected improvements in the monitoring effort have not yet taken place.

DEPARTMENT OF MENTAL HEALTH AND MENTAL RETARDATION

(73) Administrative Services

Medical Assistance Program
CFDA # 93.778 Questioned Costs: None

Finding: Inadequate review of Medicaid waiver payments

The Department of Mental Health and Mental Retardation (DMHMR)uses a network of service providers to assist individual participants in the Medicaid waiver program for the mentally retarded. DMHMR established hourly and daily reimbursement rates for each participant. For each provider, the DHS Bureau of Medical Services (BMS) enters the highest rate established for any individual assigned to that provider into the Maine Medicaid Management Information System (MMIS). Because only the highest rate is entered in the system, the provider could be reimbursed at higher rates than those approved. The providers bill BMS directly for services provided without any prior review or further approval by DMHMR.

DMHMR relies on subsequent monitoring by the three regional offices to ensure that waiver services are paid at the approved rates. The regional offices receive a quarterly report from BMS to do this; however, the report format is not readily usable for this purpose. Consequently, personnel rely on information obtained from service providers. In addition, regional personnel did not fully understand how the rates were established and claims processed by MMIS.

DEPARTMENT OF MENTAL HEALTH AND MENTAL RETARDATION

Recommendation:

To ensure that only authorized services and rates are paid to providers, we recommend that DMHMR:

- document monitoring procedures,
- document and periodically review the monitoring results, and
- advise monitoring personnel of the information available.

Auditee Response:

The Department currently has 1,150 plus clients on the Waiver and a quarterly report is issued by DHS of actual payments for services rendered. The Department's options under the current system would be to compare our Waiver tracking system to the DHS quarterly reports. The Department has spot checked the quarterly report in the past and found insignificant errors. The Department will work with DHS in the future to see if we can come up with a better solution of actual costs paid versus rates established.

DEPARTMENT OF TRANSPORTATION

(74) Bureau of Planning, Research and Community Services

Highway Planning and Construction
CFDA # 20.205 Questioned Costs: $1,567

Finding: No approved agreement for third party services

Prior written approval of the awarding agency is required when obtaining the services of a third party (49 CFR 18.30).

A Metropolitan Planning Organization (MPO) obtained services for a total cost of $429 without prior approval from the Maine Department of Transportation (MDOT). We question the $343 Federal share.

A second MPO obtained services for a traffic study after the termination date of the agreement. Because there was no approved agreement for the period covered by services, we question $1,224, the Federal share of the cost charged.

Recommendation:

We recommend that MDOT review its controls to ensure that MPO's do not engage third party services without prior written approval.

Auditee Response:

MDOT concurs and will review the use of third party services within the MPO program.

(75) Bureau of Project Development Construction Division

Federal Highway Administration
CFDA # 20.205 Questioned Costs: None

Finding: Grant progress reports not submitted

The Maine Department of Transportation (MDOT) received a Special Purpose Grant from the U.S. Department of Housing and Urban Development for a transportation study. The grant required that MDOT "submit a progress report every six months, due on June 30 and December 30 of each year."

No evidence could be found that the required reports were submitted.

Recommendation:

We recommend that MDOT meet reporting requirements.

Auditee Response:

MDOT concurs.

(76) Bureau of Project Development Construction Division

Federal Highway Administration
CFDA # 20.205 Questioned Costs: $13,600

Finding: Incorrect procedures for recording stockpiled materials

For three projects, the Maine Department of Transportation (MDOT) did not identify materials by item number, as required by the MDOT Construction Manual. Consequently, we were unable to determine the nature or quantity of all items stockpiled and could not determine compliance with 23 CFR 122 (a) (3), which limits the quantity and value of stockpiled material. Additionally, for one of the three projects, $13,600 of materials was not supported by receipted bills, as required by 49 CFR 18.20 (6).

Recommendation:

We recommend that MDOT require Construction Managers to comply with required procedures.

Auditee Response:

MDOT will review the situation and make process corrections as necessary.

(77) Bureau of Finance and Administration
Bureau of Project Development
Right of Way Division

Federal Highway Administration
CFDA # 20.205 Questioned Costs: None

Finding: Failure to adhere to contract agreements

The Maine Department of Transportation (MDOT) and the City of Lewiston entered into an agreement on August 30, 1994, for improvements to Lisbon Street. The agreement required the City of Lewiston to provide to MDOT a "right-of-way map or similar plan. . .detailing all right-of-way so acquired for the project." No such map or plan could be located at MDOT.

Recommendation:

We recommend that MDOT obtain a right-of-way map for the files.

Auditee Response:

MDOT concurs. The situation has been discussed with the staff from the Right of Way Division and appropriate action will be taken.

(78) Office of Passenger Transportation

Various Federal Programs
CFDA # Various Questioned Costs: $872,878

Finding: Charges made without documentation

Office of Management and Budget, Circular A-87 *Cost Principles for State, Local and Indian Tribal Governments*, requires that expenditures of Federal funds be made in accordance with the basic guidelines for allowability and allocation.

A journal voucher dated May 17, 1996, adjusted the Ferry Service by $872,878 and charged the expenditure to Federal funds. The journal did not provide any detail of the transaction, and no explanation was available. We therefore could not determine if the charge was allowable or properly allocated.

Recommendation:

We recommend that all charges be supported by adequate documentation.

Auditee Response:

MDOT concurs. All future financial transactions will be fully documented.

OFFICE OF THE TREASURER OF STATE

(79) Administration Division

Various Federal Programs
CFDA# Various | Questioned Costs: None

Finding: Internal control not adequate to ensure compliance with Cash Management Improvement Act

Text of finding can be found on page 100.

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State of Maine
Summary of Unresolved Material
Findings and Reportable Conditions
For the Years Ended Prior to June 30, 1996

Material findings and reportable conditions which have not received corrective action are restated as referenced below. Other significant or material findings have either been resolved or are no longer applicable in the current year.

Agency/Finding	Report Finding 1995	Report Finding 1996
Department of Administrative and Financial Services		
Insufficient procedures and resources for external financial reporting	A	A
Department of Administrative and Financial Services - Bureau of Alcoholic Beverages and Lottery Operations		
No independent verification of lottery data from vendor	B	E
Department of Administrative and Financial Services - Bureau of General Services		
Fixed asset records incomplete	C	C
Department of Administrative and Financial Services		
Inadequate internal control system in place to identify capital leases	D	D

State of Maine
Summary of Unresolved Material
Findings and Reportable Conditions
For the Years Ended Prior to June 30, 1996

Agency/Finding	Report Finding 1995	Report Finding 1996
Department of Administrative and Financial Services - Bureau of Accounts and Control		
External payment interface disbursements of $15.3 million were not recorded in the State's financial records	3	B
Department of Education - Division of School Business Services		
General Fund School Construction Money expended with inadequate oversight	11	3
Department of Human Services - Office of Management and Budget		
General Fund not reimbursed for $982,320 in expenditures	15	4
Department of Human Services - Office of Management and Budget		
General Fund due $823,160	16	5
Department of Labor - Bureau of Employment Security		
Inadequate internal control and accounting procedures for the Employment Security Trust Fund taxes receivable balance	17	6

Report Finding

State of Maine
Summary of Unresolved Material
Findings and Reportable Conditions
For the Years Ended Prior to June 30, 1996

Agency/Finding	1995	1996
Department of Labor - Office of Administrative Services		
Revenue recognition criteria not observed	20	8
Department of the Treasurer of State		
Inadequate internal control and accounting procedures over trust and agency funds	21	11

State of Maine
Unresolved Prior Year Questioned Costs
As of June 30, 1996

Year	State Agency & Federal Program	Finding Number	Federal Agency	CFDA Number	Amount
	Administrative & Financial Services				
1992	Various Federal Programs	1	Various	Various	$5,800,000
1993	Various Federal Programs	39	Various	Various	3,600,000
	Total Administrative & Financial Services				$9,400,000
	Defense & Veterans Services				
1995	Disaster Assistance	31	Emg. Mgmt.	83.516	$1,312
	Total Defense & Veterans Services				$1,312
	Economic & Community Development				
1991	Community Development Block Grant	32	HUD	14.228	$12,526
1992	Community Development Block Grant	25	HUD	14.228	18,867
1992	Community Development Block Grant	23	HUD	14.228	14,500
1994	Community Development Block Grant	23	HUD	14.228	20,193
1995	Community Development Block Grant	36	HUD	14.228	39
1995	Community Development Block Grant	38	HUD	14.228	77,510
1995	Community Development Block Grant	39	HUD	14.228	713
1995	Community Development Block Grant	40	HUD	14.228	3,000
	Total Economic & Comm. Development				$147,348
	Education				
1992	Various Federal Programs	40	ED	Various	$56,823
1993	Various Federal Programs	57	Various	Various	324,757
1994	Title I Grants - LEA'S	31	ED	84.010	20,638
1994	Various Federal Programs	1	Various	Various	335,109
	Total Education				$737,327
	Human Services				
1990	Food Stamps - Admin	92	USDA	10.561	$1,810
1990	Child Support Enforcement	88	HHS	93.563	141,174

State of Maine
Unresolved Prior Year Questioned Costs
As of June 30, 1996

Year	State Agency & Federal Program	Finding Number	Federal Agency	CFDA Number	Amount
1990	Vocational Rehabilitation Services	98	ED	84.126	1,460
1991	Food Stamps	95	USDA	10.551	2,441
1992	Various Federal Programs	45	Various	Various	83,387
1993	Social Security - Disability Insurance	69	HHS	93.802	135,822
1993	Various Federal Programs	81	Various	Various	506,698
1994	Vocational Rehabilitation Services	6	ED	84.126	99,641
1994	Social Security - Disability Insurance	46	HHS	93.802	132,488
1994	Various Federal Programs	55	Various	Various	35,035
1995	Food Stamps	58	AGRI	10.551	13,285
1995	Child Support Enforcement	64	HHS	93.563	423
1995	Payments to States for Child Care Asst.	51	HHS	93.575	312
1995	Foster Care - Title IV-E	54	HHS	93.658	195
1995	Various Federal Programs	81	Various	Various	343,915
	Total Human Services				$1,498,086
	Maine State Retirement				
1992	Various Federal Programs	97	Various	Various	$248,483
	Total Maine State Retirement				$248,483
	Transportation				
1995	Indian Affairs	100	DOT	Various	$48,534
	Total Transportation				$48,534
	Total				$12,081,090

Note: A. Questioned costs are resolved when:
1. The Federal grantor agency has determined that the funds do not have to be repaid.
2. The State has paid the Federal grantor the agreed upon amount.

B. For the complete Federal program name see the Schedule of Federal Financial Assistance.

C. The Maine State Retirement System became a public instrumentality as of December 1993 and is now considered a component unit of the State of Maine.

State of Maine
Summary of Questioned Costs
By Federal Agency
For the Year Ended June 30, 1996

Federal Grantor Agency	CFDA Number	State Agency	Amount	Finding Number
U.S. Dept. of Agriculture	10.557	Human Services	$ 1,402	47
Total U.S. Dept. of Agriculture			1,402	
U.S. Dept. of Education	84.027	Education	122,000	25
	84.048	Education	70,184	23
	84.126	Education	50,339	17
Total U.S. Dept. of Education			242,523	
Federal Highway Administration	20.205	Transportation	1,567	74
	20.205	Transportation	13,600	76
Total Federal Highway Administration			15,167	
U.S. Dept. of Health & Human Services	93.959	Executive Department	1,588	29
	93.959	Executive Department	77	30
	93.959	Executive Department	689	31
	93.959	Executive Department	114,553	28
	93.658	Human Services	125	36
	93.778	Human Services	114,582	59
Total U.S. Dept. of Health & Human Serv.			231,614	
U.S. Dept. of Housing & Urban Development	14.228	Economic & Community Dev.	649,545	15
	14.228	Economic & Community Dev.	308,204	16
Total U.S. Dept. of Housing & Urban Dev.			957,749	
Various	Various	Admin. & Financial Services	639,000	14
Various	Various	Transportation	872,878	78
Total Various			1,511,878	
Total			$2,960,333	

State of Maine
Summary of Questioned Costs
By State Agency
For the Year Ended June 30, 1996

State Agency	CFDA Number	Federal Agency	Amount	Finding Number
Dept. of Administrative & Financial Services	Various	Various	$639,000	14
Total Dept. of Admin. & Financial Serv.			639,000	
Dept. of Economic and Community	14.228	Housing & Urban Dev.	649,545	15
Development	14.228	Housing & Urban Dev.	308,204	16
Total Dept. of Economic & Community Development			957,749	
Dept. of Education	84.027	Education	122,000	25
	84.048	Education	70,184	23
	84.126	Education	50,339	17
Total Dept. of Education			242,523	
Executive Department	93.959	Health & Human Services	1,588	29
	93.959	Health & Human Services	77	30
	93.959	Health & Human Services	689	31
	93.959	Health & Human Services	114,553	28
Total Executive Department			116,907	
Dept. of Human Services	10.557	Agriculture	1,402	47
	93.658	Health & Human Services	125	36
	93.778	Health & Human Services	114,582	59
Total Dept. of Human Services			116,109	
Dept. of Transportation	20.205	Federal Highway Admin.	1,567	74
	20.205	Federal Highway Admin.	13,600	76
	Various	Various	872,878	78
Total Dept. of Transportation			888,045	
Total			$2,960,333	

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