STATE OF MAINE

MANAGEMENT LETTER
to the Annual Comprehensive Financial Report
Fiscal Year Ending June 30, 2021

Office of the State Auditor
Jacob B. Norton, CIA
State Auditor

State of Maine
Management Letter to the Annual Comprehensive Financial Report
Fiscal Year Ending June 30, 2021

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**This finding has been redacted consistent with Government Auditing Standards, also known as the Yellow Book (Chapter 6, Standards for Financial Audits, Reporting Confidential or Sensitive Information, Requirements: Reporting Confidential or Sensitive Information, paragraphs 6.63 through 6.65)*

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Jacob B. Norton, CIA
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B. Melissa Perkins, CPA
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LETTER OF TRANSMITTAL

Honorable Members of the Legislative Council for the 130th Legislature

Honorable Janet T. Mills
Governor of the State of Maine

I am pleased to submit the State of Maine Management Letter related to our audit of the State's Annual Comprehensive Financial Report for the year ended June 30, 2021. In the course of conducting this audit, we became aware of matters that offer opportunities for our government to improve its operations. Recommendations regarding these matters accompany this Management Letter as "management letter comments." A separate Management Letter will be issued this spring following the conclusion of the Single Audit for the year ended June 30, 2021.

I welcome your thoughts and inquiries about these matters.

Respectfully submitted,

Jacob B. Norton, CIA
State Auditor

January 27, 2022

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B. Melissa Perkins, CPA
Acting State Auditor

MANAGEMENT LETTER TO THE ANNUAL COMPREHENSIVE FINANCIAL REPORT

Honorable Members of the Legislative Council for the 130th Legislature

Honorable Janet T. Mills
Governor of the State of Maine

In planning and performing our audit of the financial statements of the State of Maine as of and for the year ended June 30, 2021, on which we have issued our report dated December 10, 2021, in accordance with auditing standards generally accepted in the United States of America, we considered the State of Maine's internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the State of Maine's internal control. Accordingly, we do not express an opinion on the effectiveness of the State of Maine's internal control. This report is based on our knowledge as of the date of our report on the financial statements, obtained in performing our audit thereof, and should be read with that understanding.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all weaknesses or deficiencies in internal control. Given these limitations, not all weaknesses or deficiencies in controls may have been identified. However, during our audit, we became aware of certain matters that resulted in "management letter comments" which are presented for your consideration and offer opportunities for strengthening internal control and improving operating procedures of the State of Maine. These matters were not identified as material weaknesses or significant deficiencies in a separate report titled Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*. The following pages contain our comments and suggestions regarding those matters.

One of the three management letter comments is redacted because it relates to confidential and sensitive information. Redacting this information is consistent with *Government Auditing Standards* promulgated by the U.S. Government Accountability Office.

This communication is intended solely for the information and use of the Legislature, the Governor, and others within State government, and is not intended to be, and should not be, used by anyone other than these specified parties.

We would be pleased to discuss these management letter comments in further detail at your convenience.

B.M. Perkins

B. Melissa Perkins, CPA
Acting State Auditor

December 10, 2021

DEPARTMENT OF ADMINISTRATIVE AND FINANCIAL SERVICES

ML-21-0104-01

Title: Financial reporting procedures need improvement

State Department: Administrative and Financial Services
State Bureau: Office of the State Controller

Type of Finding: Management letter

Criteria: Governmental Accounting, Auditing, and Financial Reporting (GAAFR), Part 5, Section A, Chapter 42; Governmental Accounting Standards Board (GASB) Concept Statement 1, paragraph 64

The GAAFR states that a comprehensive framework of internal control is required to obtain reasonable assurance over financial reporting.

GASB Concept Statement 1 states that financial reporting should be reliable.

Condition: The State of Maine's Annual Comprehensive Financial Report (ACFR) for the fiscal year ending June 30, 2021 prepared by the Office of State Controller (OSC) included the following misstatements and errors identified by the Office of the State Auditor (OSA):

- Revenues and expenses in the Internal Service Funds were overstated by $97.4 million.
- Note disclosures and Management's Discussion and Analysis (MD&A) contained incorrect amounts and excluded required information.

OSC subsequently adjusted these amounts and disclosures in the ACFR.

Context: The ACFR provides financial and other information about State government to the general public, investors and other interested groups. It provides valuable insight into how State government officials manage public funds. The ACFR also provides information used by credit rating services to assess the State's fiscal integrity. This assessment results in the assignment of a credit rating to State of Maine government bonds, which affects the interest rate the State must pay to borrow money.

Cause: Lack of financial reporting procedures to ensure closing entries and disclosures are complete and accurate

Effect: The financial statements and related disclosures could contain significant errors and omissions.

Recommendation: We recommend that OSC implement financial reporting procedures to ensure that significant errors and omissions in the ACFR are prevented, or detected and corrected, prior to release for audit by OSA.

Management's Response: The OSC acknowledges that an undetected human error resulted in an incorrect adjustment being made to the ACFR. This resulted in revenue and expenses being overstated with no impact on net position. OSC will continue to work diligently and evaluate our analytical review procedures to ensure that similar issues are prevented in the future.

Contact: April Newman, Financial Management Coordinator, OSC, 207-626-8436

ML-21-0320-02

Title: Accounting procedures over capital building leases need improvement

State Department: Administrative and Financial Services
State Bureau: General Government Service Center

Type of Finding: Management letter

Criteria: Governmental Accounting Standards Board (GASB) Codification L.20.111

The Codification requires that a lessee record a capital lease as an asset and an obligation at an amount equal to the present value of the future minimum lease payments at the beginning of the lease term or the fair value of the asset at lease inception, whichever is less.

Condition: Lease accounting procedures used by the General Government Service Center (GGSC) require building leases to be valued at the lesser of the discounted net present value of the future minimum lease payments at the beginning of the lease term or the fair market value of the lease asset. The GGSC establishes the fair market value of the leased building by using the town's or city's tax assessment plus the value of subsequent building permits, or by using an assessment provided by the landlord. There are no control procedures among the GGSC's procedures to determine whether the amount resulting from this calculation represents the fair value of the property at lease inception.

Context: The Department manages capital leases totaling $43 million in assets, net of accumulated depreciation, and $48 million in lease liabilities.

Cause: The Department does not have procedures in place to ensure the proper valuation of leased space when the local municipality's valuation may not be reflective of fair value.

Effect: Capital assets and lease obligations may not be correctly valued. As a result, assets and liabilities, and lease amortization and depreciation expense may be understated or overstated in the State's financial statements.

Recommendation: We recommend that the Department revise lease accounting procedures to include an option for proactively obtaining an independent private sector appraisal to support the valuation of major leased property at lease inception when the municipality's valuation does not appear reasonable or when it does not appear to be adequately substantiated.

Management's Response: The Department does not agree with the recommendation to obtain independent private sector appraisals. Management is required to estimate the fair value of the leased asset at the lease inception date. It is our practice to utilize tax assessments as a basis for estimates. We have found that this basis for estimating fair value is objective, well documented, reliable, and cost effective.

Contact: Janre Mullins, Director, General Government Service Center, DAFS, 207-624-7399

Auditor's Concluding Remarks: The Office of the State Auditor agrees that using a tax assessment as the basis for estimating fair value is often an objective, reliable and cost-effective method. However, the tax assessment is not the same as fair value and may differ significantly. Implementing policies which require a market appraisal when there is indication that the tax assessment may not be a reliable representation of fair market value will ensure that the Department is valuing leased property in accordance with GASB pronouncements.

The finding remains as stated.

ML-21-0903-02, Confidential, see below for more information

Title: ________ over ________ and ________ of ________ for the ________, ________ and ________ systems needs improvement

Pursuant to paragraph 6.63 of the U.S. Government Accountability Office's Government Auditing Standards (also known as the Yellow Book), we omitted details from this finding as they are confidential under the provisions of 5 MRSA 244-C (3). Though the content of this finding has been redacted, which appears as blank underlining, we provided the Department(s) with detailed information regarding the specific condition we identified, as well as the related criteria, context, causes, effects, and our specific recommendations for improvement.

State Department: Administrative and Financial Services
State Bureau: Human Resources

Type of Finding: Management letter

Criteria: ________

Condition: ________

Context: ________

Cause: ________

Effect: ________

Recommendation: ________

Management's Response: ________

Contact: Shonna Poulin-Gutierrez, Executive Director, Employee Health & Wellness, DAFS, 207-624-7367