



OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

Financial-Related Audit

Office of Administrative Hearings
July 1, 1995, through June 30, 2000



Financial Audit Division

The Office of the Legislative Auditor (OLA) is a professional, nonpartisan office in the legislative branch of Minnesota State government. Its principal responsibility is to audit and evaluate the agencies and programs of state government (the State Auditor audits local governments).

OLA's Financial Audit Division annually audits the state's financial statements and, on a rotating schedule, audits agencies in the executive and judicial branches of state government, three metropolitan agencies, and several "semi-state" organizations. The division also investigates allegations that state resources have been used inappropriately.

The division has a staff of approximately fifty auditors, most of whom are CPAs. The division conducts audits in accordance with standards established by the American Institute of Certified Public Accountants and the Comptroller General of the United States.

Consistent with OLA's mission, the Financial Audit Division works to:

- Promote Accountability,
- Strengthen Legislative Oversight, and
- Support Good Financial Management.

Through its Program Evaluation Division, OLA conducts several evaluations each year and one best practices review.

OLA is under the direction of the Legislative Auditor, who is appointed for a six-year term by the Legislative Audit Commission (LAC). The LAC is a bipartisan commission of Representatives and Senators. It annually selects topics for the Program Evaluation Division, but is generally not involved in scheduling financial audits.

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OFFICE OF THE LEGISLATIVE AUDITOR
State of Minnesota • James Nobles, Legislative Auditor

Senator Ann Rest, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

The Honorable Kenneth Nickolai
Chief Administrative Law Judge
Office of Administrative Hearings

We have audited the financial activities of the Office of Administrative Hearings for the period July 1, 1995, through June 30, 2000. Our audit scope included financial management, administrative law fees, payroll, and administrative expenditures. The audit objectives and conclusions are highlighted in the individual chapters of this report.

We conducted our audit in accordance with generally accepted auditing standards and Government Auditing Standards, as issued by the Comptroller General of the United States. Those standards require that we design the audit to provide reasonable assurance that the Office of Administrative Hearings complied with provisions of laws, regulations, and contracts that are significant to the audit. The office's management is responsible for establishing and maintaining the internal control structure and complying with applicable laws, regulations, and contracts.

This report is intended for the information of the Legislative Audit Commission and the management of the Office of Administrative Hearings. This restriction is not intended to limit the distribution of this report, which was released as a public document on April 5, 2001.

/s/ James R. Nobles

James R. Nobles
Legislative Auditor

/s/ Claudia J. Gudvangen

Claudia J. Gudvangen, CPA
Deputy Legislative Auditor

End of Fieldwork: February 14, 2001

Report Signed On: April 2, 2001

Office of Administrative Hearings

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Audit Participation

The following members of the Office of the Legislative Auditor prepared this report:

Claudia Gudvangen, CPA	Deputy Legislative Auditor
Jeanine Leifeld, CPA, CISA	Audit Manager
Scott Tjomsland, CPA	Auditor-in-Charge
Tim Haag	Auditor

Exit Conference

We discussed the findings and recommendations included in this report with the following representatives of the Office of Administrative Hearings at an exit conference held on March 23, 2001:

Kenneth Nickolai	Chief Administrative Law Judge
Susan Schleisman	Administrative Officer
Dennis Reek	Accounting Supervisor

Report Summary

Key Findings and Recommendations:

- In some cases, the Office of Administrative Hearings (office) did not appropriately allocate costs between its various funding sources. The office's two main sources of funding are the Workers' Compensation Special Compensation Fund and the Administrative Hearings Fund. We found several instances where the office did not charge expenditures to the appropriate funding source. The office should correct any allocation errors between the two funding sources and cancel the resulting prior year balances, as appropriate. The office should charge the payroll and business expense reimbursement expenditures to the appropriate funding source based on actual activity and consistently charge recurring expenditures to the appropriate funding source, or document reasons that justify deviations from normal funding sources. (Finding 1, page 6)
- The office did not adequately segregate duties related to processing payroll and to collecting, depositing, and recording administrative law fees. The office should segregate duties relating to these functions, or establish mitigating controls, such as an independent review of the employee's work. (Findings 2 and 3, pages 10 and 13)
- The office did not comply with the state's special expense policy when making certain food and supply purchases. The office should update its special expense plan and procedures and submit it to the Department of Employee Relations for approval. The office should implement a process to ensure it complies with the state's special expense policy. (Finding 4, page 13)

Background:

The Legislature established the Office of Administrative Hearings in 1976 to provide a fair, prompt, and impartial hearing process for citizens who disagree with actions taken by government. The office consists of two separate divisions: the Administrative Law Division and the Workers' Compensation Division. The Administrative Law Division hears state agency Administrative Procedure Act cases, rulemaking cases, and local government licensing and personnel cases. The Workers' Compensation Division conducts workers' compensation settlement conferences and hears workers' compensation benefit cases.

Office of Administrative Hearings

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Office of Administrative Hearings

Chapter 1. Introduction

The Legislature established the Office of Administrative Hearings in 1976 to provide a fair, prompt, and impartial hearing process for citizens who disagree with actions taken by government. In 1982, the Legislature transferred the workers' compensation benefit hearing function to the Office of Administrative Hearings. In 1987, the office began hearing child support award cases. However, in January 1999, the Supreme Court determined it was unconstitutional for the office to perform child support hearings. As a result, that function transferred from the office to the court system on October 1, 1999. On July 1, 1998, the workers' compensation settlement function transferred from the Department of Labor and Industry to the office based on legislation that eliminated the distinction between the workers' compensation benefit hearing and settlement functions.

The office consists of two separate divisions: the Administrative Law Division and the Workers' Compensation Division. The Administrative Law Division hears state agency Administrative Procedure Act cases, rulemaking cases, and local government licensing and personnel cases. The Workers' Compensation Division conducts workers' compensation settlement conferences and hears workers' compensation benefit cases. The Administrative Law Division bills government units for which it conducts services at an hourly rate plus expenses to cover its costs. The Legislature funds the activity of the Workers' Compensation Division through appropriations from the Workers' Compensation Special Compensation Fund. The office also collects fees to cover its costs for the preparation of the record of proceedings for submission to the workers' compensation court of appeals and for the preparation of transcripts.

The office maintains its main office in Minneapolis for the Administrative Law Division and the majority of the Workers' Compensation Division, but also maintains satellite offices for the Workers' Compensation Division in St. Paul, Duluth, and Detroit Lakes. A Chief Administrative Law Judge, who is appointed by the Governor for a six-year term, heads the office. Kenneth Nickolai, the current Chief Administrative Law Judge, served as the acting Chief Administrative Law Judge from November 1997 until beginning his six-year appointment on July 1, 1998. Kevin Johnson, the former Chief Administrative Law Judge, served from July 1993 until November 1997.

Office of Administrative Hearings

Table 1-1 shows the financial activity of the office for fiscal year 2000.

Table 1-1
Financial Activity for Fiscal Year 2000

Sources:	Workers' Comp Fund	Administrative Hearings Fund	Workers' Comp Transcript Fund
Appropriations	\$6,664,000	\$ 400,000 ⁽¹⁾	\$ 0
Balance Forward In	0	1,219,199	56,383
Transfers In	189,000	0	0
Receipts	0	1,936,219	8,730
Total	<u>\$6,853,000</u>	<u>\$3,555,418</u>	<u>\$65,113</u>
Uses:			
Payroll	\$5,578,373	\$1,451,447	\$ 0
Professional/Technical Services	93,244	626,488	3,043
Rent	464,425	255,120	0
Communications	134,369	41,449	0
Travel and Employee Development	93,833	33,423	0
Computer and Systems Services	103,142	8,566	0
Equipment	100,285	3,580	0
Supplies	79,637	15,218	0
Other Expenditures/Expenses	63,261	68,756	2,713
Balance Forward Out	142,431	1,051,371	59,357
Total	<u>\$6,853,000</u>	<u>\$3,555,418</u>	<u>\$65,113</u>

Note 1: General Fund appropriation to help offset the loss of revenue from the transfer of the child support hearing function from the office to the court system in fiscal year 2000.

Source: Minnesota Accounting and Procurement System.

Chapter 2. Financial Management

Chapter Conclusion

The office appropriately transferred resources related to the shift of workers' compensation and child support functions to and from the office and properly accounted for the transfers. However, we found that the office did not appropriately allocate certain costs between its various funding sources. We also noted that, due to an error in redepositing a prior year recovery, the office had \$32,474 more available to spend from the Workers' Compensation Special Compensation Fund during fiscal year 1998 than it was appropriated.

The office receives annual appropriations from the Workers' Compensation Special Compensation Fund for its Workers' Compensation Division activities. Unused portions of the appropriations carry forward from the first year to the second year of a biennium, but cancel at the end of the biennium. The appropriations for fiscal years 1996 and 1997 earmarked \$100,000 each year for an internship program and \$180,000 each year for additional clerical support for workers' compensation judges. The fiscal year 1996 appropriation also earmarked \$125,000 for a calendaring system. Table 2-1 shows the annual activity for the appropriations for fiscal years 1996 to 2000.

Table 2-1
Workers' Compensation Special Compensation Fund Appropriation Activity
Fiscal Years 1996 to 2000

	1996	1997	1998	1999	2000
Appropriation	\$3,946,000	\$3,826,000	\$4,107,000	\$4,195,000	\$6,664,000
Balance Forward In	0	392,297	0	150,429	0
Transfers In	80,470	163,188	0	2,251,898 ⁽²⁾	189,000 ⁽⁴⁾
Expenditures	3,634,173	4,114,685	3,956,571 ⁽¹⁾	6,589,169	6,710,569
Balance Forward Out	<u>\$ 392,297</u>	<u>\$ 0</u>	<u>\$ 150,429</u>	<u>\$ 0</u>	<u>\$ 142,431</u>
Canceled	<u>\$ 0</u>	<u>\$ 266,800</u>	<u>\$ 0</u>	<u>\$ 8,158⁽³⁾</u>	<u>\$ 0</u>

Note 1: Expenditures are understated by \$32,474. The office erroneously paid two invoices twice at the end of fiscal year 1997, but did not collect the overpayment until after the fiscal year closed. The office recorded the receipt of the overpayment as an expenditure reduction in fiscal year 1998.

Note 2: Transfer from the Department of Labor and Industry to pay for the activity of the workers' compensation settlement function, which transferred from the Department of Labor and Industry to the office on July 1, 1998. The office set up a separate appropriation account for the transfer.

Note 3: \$6,414 canceled from the office appropriation and \$1,744 canceled from the transferred funds from the Department of Labor and Industry.

Note 4: Transfer from the Department of Administration for a small agency infrastructure project. The office set up a separate appropriation account for the transfer.

Source: Minnesota Accounting and Procurement System.

Office of Administrative Hearings

Minn. Stat. Section 14.53 authorizes the office to bill government units for the cost of services rendered by its Administrative Law Division. Minn. Stat. Section 14.54 established the Administrative Hearings Fund for the office to use as a revolving account for the activities of its Administrative Law Division. The office deposits its Administrative Law Division receipts into the fund and uses those receipts to pay the costs of its Administrative Law Division activity. Table 2-2 shows the annual activity for the Administrative Hearings Fund for fiscal years 1996 to 2000.

Table 2-2
Administrative Hearings Fund Activity
Fiscal Years 1996 to 2000

	1996	1997	1998	1999	2000
Beginning Balance	\$ 384,292	\$ 473,665	\$ 735,656	\$ 800,768	\$1,219,199
Receipts	2,907,734 ⁽¹⁾	3,955,149	4,908,591	5,211,190	1,936,219
Expenditures	<u>2,818,361</u>	<u>3,693,158</u>	<u>4,843,479⁽²⁾</u>	<u>4,792,759</u>	<u>2,298,793</u>
Ending Balance	<u>\$ 473,665</u>	<u>\$ 735,656</u>	<u>\$ 800,768</u>	<u>\$1,219,199</u>	<u>\$ 856,625</u>

Note 1: Includes transfer in of \$50,000.

Note 2: Includes transfer out of \$35,000.

Source: Minnesota Accounting and Procurement System.

The office lost a significant source of revenue for its Administrative Law Division when the child support hearing function transferred to the court system in fiscal year 2000. As a result, the office may have to significantly increase its Administrative Law Division billing rates in the next biennium. To help offset the loss of revenue from the transfer, the Legislature gave the office a General Fund appropriation of \$400,000 for fiscal year 2000. The office expended \$205,254 of the appropriation during fiscal year 2000 and carried the remaining \$194,746 forward to fiscal year 2001.

Minn. Stat. Section 176.421 authorizes the office to collect a fee for the preparation of records of proceedings for submission to the workers' compensation court of appeals and for the preparation of transcripts. The statute also established the Workers' Compensation Transcript Fund for the office to use as a revolving account for that activity. Table 2-3 shows the annual activity for the Workers' Compensation Transcript Fund for fiscal years 1996 to 2000.

Table 2-3
Workers' Compensation Transcript Fund Activity
Fiscal Years 1996 to 2000

	1996	1997	1998	1999	2000
Beginning Balance	\$30,046	\$38,376	\$45,643	\$52,060	\$56,383
Receipts	17,201	13,594	11,660	9,806	8,730
Expenditures	<u>8,871</u>	<u>6,327</u>	<u>5,243</u>	<u>5,483</u>	<u>5,756</u>
Ending Balance	<u>\$38,376</u>	<u>\$45,643</u>	<u>\$52,060</u>	<u>\$56,383</u>	<u>\$59,357</u>

Source: Minnesota Accounting and Procurement System.

Office of Administrative Hearings

Audit Objectives and Methodology

We focused on the following objectives during our audit of the office's financial management:

- Did the office charge expenditures to the appropriate funding source?
- Did the office use funds earmarked for specific purposes as intended?
- Were transfers of resources related to the shift of functions to and from the office appropriate and properly accounted for?

To answer these questions, we interviewed office staff to gain an understanding of the procedures to assign expenditures to specific funding sources. We reviewed expenditures to determine if they were charged to appropriate funding sources and to determine if the office used earmarked funds as intended. Finally, we reviewed the procedures to transfer the workers' compensation settlement function to the office from the Department of Labor and Industry and to transfer the child support hearing function from the office to the court system.

Conclusions

The office appropriately transferred resources related to the shift of functions to and from the office and properly accounted for the transfers. However, as discussed in Finding 1, we found that the office did not appropriately allocate certain costs between its various funding sources.

We also noted that, due to an error in redepositing a prior year recovery, the office had \$32,474 more available to spend from the Workers' Compensation Special Compensation Fund during fiscal year 1998 than it was appropriated. Actual expenditures for the 1998 – 1999 biennium were understated by \$32,474 due to duplicate payments at the end of fiscal year 1997 that the office recovered and recorded as an expenditure reduction in fiscal year 1998. Since the fiscal year 1997 appropriation canceled at the end of that fiscal year, the office did not have the authority to spend the recovered overpayments during fiscal years 1998 and 1999. However, the office canceled only \$6,414 from the appropriations at the end of fiscal year 1999 and spent the remaining recovered amount.

1. The office did not charge certain expenditures to the appropriate funding source.

In some cases, the office did not appropriately allocate certain costs between its various funding sources. The office's two main sources of funding are the Workers' Compensation Special Compensation Fund and the Administrative Hearings Fund. Appropriations from the Workers' Compensation Fund are intended for hearing workers' compensation claims and settlements. Dedicated receipts from the Administrative Hearings Fund revolving account, established under Minn. Stat. Section 14.54, are for the office's administrative law duties.

We found several instances where the office did not charge expenditures to the appropriate funding source:

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- The office inappropriately charged \$11,400 in payroll and business expense reimbursements for an administrative law judge to the workers' compensation appropriation. As an administrative law judge, the employee did not perform any workers' compensation duties. The employee went on a mobility assignment to the Hennepin County Public Defender's Office from March 1997 to January 1999. At the start of the mobility assignment through the end of fiscal year 1997, the office charged half the employee's payroll and business expenses to the workers' compensation appropriation. Prior to the mobility assignment, and again beginning in fiscal year 1998 through the end of the assignment, the office charged all of the employee's payroll expenditures to the Administrative Hearings Fund. Also, the office deposited reimbursements it received from Hennepin County as compensation for the mobility assignment into the Administrative Hearings Fund.
- The office inappropriately charged \$1,772 of an employee's business expense reimbursements during fiscal years 1999 and 2000 to the workers' compensation appropriation. The employee served as both an administrative law judge and the information technology supervisor for the entire office. Even though most of the employee's business expenses related to the employee's work as an administrative law judge, the office charged half of the expenses to the workers' compensation appropriation. In addition, the office routinely split the employee's payroll costs equally between the Administrative Hearings Fund and the workers' compensation appropriation, without considering the employee's time spent as an administrative law judge. The office should charge the payroll and business expense costs the employee incurred during the employee's administrative law judge work to the Administrative Hearings Fund and should split the payroll expenditures related to the employee's information technology supervisor activity between the two funding sources based on reasonable criteria.
- The office did not consistently split certain monthly expenditures between the Administrative Hearings Fund and the workers' compensation appropriation. We identified six instances during fiscal years 1999 and 2000 where the office did not split monthly parking reimbursements for two administrative employees between the two funding sources consistent with other months. For five of the instances, the office charged the entire reimbursement to a single funding source. For the other instance, the office split the reimbursement in a different ratio than used in other months. The office also did not split its rent expenditures for June 1998 between the two funding sources consistent with other months of the audit period. If the office had consistently split these expenditures between the funding sources, it would have charged an additional \$2,563 to the workers' compensation appropriation instead of the Administrative Hearings Fund.
- The office changed the funding source of payroll expenditures during selected pay periods for four employees, but did not document reasons for the changes. For a single pay period in fiscal year 1996, the office charged the payroll costs for two administrative employees entirely to the workers' compensation appropriation. During the rest of the audit period, the office split the payroll expenditures for those two employees equally between the workers' compensation appropriation and the Administrative Hearings Fund.

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For two other employees that worked in the Administrative Law Division, the office charged portions of their payroll expenditures during fiscal year 1999 to the workers' compensation appropriation. Without documentation, we could not determine whether it was appropriate for the office to charge these payroll expenditures to that appropriation. If the office had charged these payroll expenditures to funding sources consistent with other pay periods, it would have charged an additional \$9,981 to the Administrative Hearings Fund instead of the workers' compensation appropriation.

Recommendations

- *The office should correct any allocation errors between the Administrative Hearings Fund and the Workers' Compensation Special Compensation Fund and cancel the resulting prior year balances, as appropriate.*
- *For the employee that serves as both an administrative law judge and the information technology supervisor, the office should charge the payroll and business expense reimbursement expenditures to the appropriate funding source based on the employee's actual activity.*
- *The office should consistently charge recurring expenditures to the appropriate funding source and should document reasons that justify deviations from normal funding sources.*

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Chapter 3. Administrative Law Fees

Chapter Conclusion

The office accurately billed agencies and local government units for administrative law services rendered. The office adequately safeguarded and promptly deposited administrative law fees and properly recorded them in the accounting records. However, we noted a lack of segregation of duties in the process to collect, deposit, and record administrative law fees.

The office bills state agencies and local government units such as cities, counties, and school districts for Administrative Law Division services. Table 2-2 shows the office's revenue for those services from fiscal year 1996 to 2000. During fiscal years 1999 and 2000, the office billed its clients \$91 per hour for administrative law judge time and \$50 per hour for staff attorney time. The rates were \$89 per hour for administrative law judge time and \$48 per hour for staff attorney time during fiscal years 1996 to 1998. The office also bills clients for business expenses, such as travel, related to the services rendered.

Generally, the office receives payments from state agencies via the inter-agency payment process within the state's accounting system. Local government units generally pay by check. During fiscal years 1996 to 1999, the office collected approximately 70 percent of its revenue by check. After the child support hearing function transferred to the court system in fiscal year 2000, the percentage of revenue collected by check decreased to approximately 15 percent.

Audit Objectives and Methodology

We focused on the following objectives during our audit of administrative law fees:

- Did the office accurately bill agencies and local government units for administrative law services rendered?
- Did the office adequately safeguard and promptly deposit administrative law fees in compliance with applicable legal provisions?
- Did the office properly record administrative law fees in the accounting records?

To answer these questions, we interviewed office staff to gain an understanding of the billing process for administrative law services, procedures to maintain and monitor accounts receivable records, and procedures to process, deposit, and record administrative law fees collected. We conducted tests to determine the accuracy of administrative law billings and related accounts

Office of Administrative Hearings

receivable records. We also reviewed receipt transactions to determine if money was promptly deposited and properly recorded.

Conclusions

The office accurately billed agencies and local government units for administrative law services. The office adequately safeguarded and promptly deposited administrative law fees and properly recorded them in the accounting records. However, as discussed in Finding 2, we noted a lack of segregation of duties in the process to collect, deposit, and record administrative law fees.

2. The office did not adequately segregate duties related to collecting, depositing, and recording administrative law fees.

A single Administrative Hearings employee is responsible for collecting, depositing, and recording incoming administrative law fees. Generally, employees responsible for maintaining accounts receivable records and recording receipts should not have physical access to the receipts. Without proper segregation, errors or irregularities could occur without detection. If a small agency, such as the office, does not have sufficient staff to adequately segregate duties, it should establish mitigating controls, such as independent review of the employee's work, to alleviate the risk caused by the lack of segregation.

Recommendation

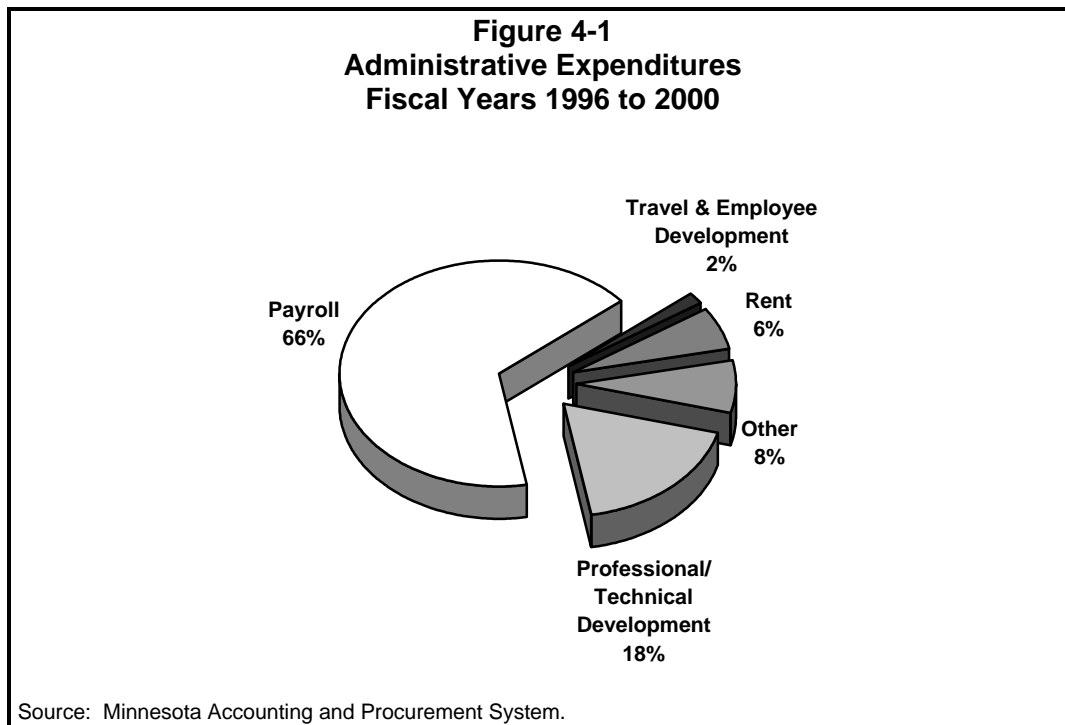
- *The office should segregate duties related to collecting, depositing, and recording administrative law fees, or establish mitigating controls to alleviate the risk.*

Chapter 4. Administrative Expenditures

Chapter Conclusion

The office properly recorded expenditures in the accounting records. However, we noted a lack of segregation of duties in the payroll process. For items tested, except for noncompliance with the state's special expense policy, the office processed and paid administrative expenditures in compliance with applicable legal provisions.

The office spent approximately \$43.7 million during fiscal years 1996 to 2000. Our review of administrative expenditures included payroll, professional/technical services, rent, and travel and employee development, which represented approximately 92 percent of the office's administrative expenditures. Figure 4-1 shows the breakdown of administrative expenditures by type.



Audit Objectives and Methodology

We focused on the following objectives during our audit of administrative expenditures:

Office of Administrative Hearings

- Did the office process and pay administrative expenditures in compliance with applicable legal provisions?
- Did the office properly record administrative expenditures in the accounting records?

To answer these questions, we interviewed office staff to gain an understanding of the payroll and personnel process, the process to obtain and pay for professional/technical services, and the process to authorize and pay travel and employee development expenditures. We reviewed payroll and personnel transactions to determine if they were processed in compliance with applicable legal provisions, and if the office properly recorded the transactions. We also tested samples of professional/technical services, travel, and employee development expenditures to determine if the office complied with applicable legal provisions and properly recorded the expenditures. Finally, we compared rent expenditures to lease agreements to determine if the office paid its rent in compliance with valid lease agreements and properly recorded the expenditures.

Payroll

The office had total payroll expenditures of approximately \$29 million during fiscal years 1996 to 2000. At the end of fiscal year 2000, the office employed about 97 individuals. Seventy of those employees worked in the Workers' Compensation Division, seventeen in the Administrative Law Division, and ten in administrative services and information technology.

Professional/Technical Services

The office spent approximately \$7.9 million on professional/technical services during fiscal years 1996 to 2000. Most of those expenditures paid for services obtained from administrative law judges, court reporters, and interpreters. The office contracted with those individuals to conduct administrative law hearings, mostly child support cases. After the child support hearing function transferred to the court system during fiscal year 2000, the office's expenditures for professional/technical services decreased significantly.

Rent

The office had rent expenditures of nearly \$2.7 million during fiscal years 1996 to 2000. The office's main office in Minneapolis housed the entire Administrative Law Division, all administrative services and information technology staff, and just over half of the Workers' Compensation Division. Most of the remaining employees in the Workers' Compensation Division worked in the St. Paul office, with five others in the Duluth office and two in the Detroit Lakes office.

The office remains liable for office space in Minneapolis that housed the child support hearing function before it transferred to the court system during fiscal year 2000. Attempts by the office to renegotiate the lease that runs through the end of fiscal year 2002 were unsuccessful, and the office has not been able to locate a tenant to sublease the space. The office will pay about \$163,000 and \$168,000 in fiscal years 2001 and 2002, respectively, for the mostly unused space.

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Travel and Employee Development

The office spent about \$652,000 on travel and employee development during fiscal years 1996 to 2000. Legal professionals employed by the office were authorized to incur up to \$2,500 each year to attend continuing education classes or conferences, often outside Minnesota. Workers' Compensation Judges and Administrative Law Judges also traveled throughout Minnesota to conduct hearings. The office paid approximately 56 percent of its travel and employee development expenditures directly to vendors, with about 44 percent paid to employees as reimbursements. The office also reimbursed employees about \$16,000 for expenses other than travel or employee development.

Conclusions

The office properly recorded expenditures in the accounting records. However, as discussed in Finding 3, we found a lack of segregation of duties in the payroll process. For items tested, the office processed and paid administrative expenditures in compliance with applicable legal provisions, except that, in Finding 4, we noted that the office did not comply with the state's special expense policy.

3. The office did not adequately segregate duties related to processing payroll.

A single employee processed all payroll expenditures, including the employee's own payroll expenditures, and no other employee reviewed those expenditures. Ideally, employees who process payroll should not be able to process their own transactions. Without proper segregation, employees could manipulate their payroll transactions to benefit themselves, without detection. If a small agency, such as the office, does not have sufficient staff to adequately segregate duties, it should establish mitigating controls to alleviate the risk caused by the lack of segregation.

Recommendation

- *The office should segregate duties related to processing payroll, or establish mitigating controls to alleviate the risk.*

4. The office did not comply with the state's special expense policy.

The office made food and supply purchases without complying with the state's special expense policy. For example, we found instances where the office reimbursed an employee for supplies for an ice cream social and for supplies for a retirement event. We found other instances where the office purchased refreshments for staff meetings. We did not find any evidence that the office obtained the proper approvals for those purchases in advance.

The Department of Employee Relations Administrative Procedure 4.4 defines certain purchases as "special expenses." In order for agencies to incur special expenses, they must either purchase in accordance with a preapproved agency special expense plan, or must have individual

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purchases approved in advance by the Departments of Finance and Employee Relations. Administrative Procedure 4.4 also states that refreshments may not be provided for routine staff meetings, and that special expenses may not be used for employee parties. The office did have a special expense plan on file with the Department of Employee Relations, submitted in 1989. However, many of the special expense purchases the office made were not allowed under its special expense plan.

Recommendation

- *The office should update its special expense plan and procedures and submit it to the Department of Employee Relations for approval. The office should implement a process to ensure it complies with the state's special expense policy.*

**Status of Prior Audit Issues
As of February 14, 2001**

Legislative Audit Report 96-30, issued in August 1996, covered the four fiscal years ending June 30, 1995. The audit scope included administrative law fees and administrative expenditures. The audit report contained one finding, concerning the recording and payment of compensatory time earned by administrative law judges. The Office of Administrative Hearings resolved the finding.

State of Minnesota Audit Follow-Up Process

The Department of Finance, on behalf of the Governor, maintains a quarterly process for following up on issues cited in financial audit reports issued by the Legislative Auditor. The process consists of an exchange of written correspondence that documents the status of audit findings. The follow-up process continues until Finance is satisfied that the issues have been resolved. It covers entities headed by gubernatorial appointees, including most state agencies, boards, commissions, and Minnesota state colleges and universities. It is not applied to audits of the University of Minnesota, any quasi-state organizations, such as metropolitan agencies or the State Agricultural Society, the state constitutional officers, or the judicial branch.

Office of Administrative Hearings

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STATE OF MINNESOTA
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March 28, 2001

James R. Nobles
Legislative Auditor
100 Centennial Office Building
658 Cedar Street
St. Paul, MN 55155

Dear Mr. Nobles:

This letter constitutes the response of the Office of Administrative Hearings to the Audit Report of the Office of the Legislative Auditor for the period from July 1, 1995 through June 30, 2000.

Finding 1. The office did not charge certain expenditures to the appropriate funding source.

A. The office has discussed the \$11,400 payroll and expenditure amounts (March 1997 to January 1999) with Merrill King, OAH's Executive Budget Office at the Department of Finance. Ms. King indicated she would provide us with advice on how the Department of Finance would prefer to handle the transaction. The office will correctly charge appropriate funding sources in the future.

Person Responsible: Dennis Reek
Completion Date: Immediate

B. The office has investigated the \$1,772 (FY 1999 and 2000) in employee business expense reimbursements. Further study has indicated that the reimbursements were inappropriately charged and we agree to reimburse the Special Compensation Fund in the amount of \$1,772.

Person Responsible: Dennis Reek
Completion Date: Immediate

C. The office has carefully evaluated the other transactions identified in this finding, and we are confident that the appropriations were properly charged for the identified monthly expenditures. However, we agree the office needs to improve its documentation of such expenditure changes and require written memos to the file or the biweekly time reports by the Chief Administrative Law Judge or his designee to provide an improved audit trail.

Person Responsible: Dennis Reek
Completion Date: Immediate

Finding 2. The office did not adequately segregate duties related to collecting, depositing, and recording administrative fees.

The office receptionist will continue to receive, open and date stamp all incoming mail. All fees received will be opened, date stamped, endorsed and given to Elizabeth Suszynski. Ms. Suszynski will then prepare the bank deposit and a log sheet listing all fees collected to be deposited. Dennis Reek will review the log sheet and deposit. Ms. Suszynski will be responsible for recording and depositing the receipts. We believe that this change in process will properly segregate the duties of collecting, depositing and recording fees in the Office and will result in controls that will minimize any risk.

Persons Responsible: Dennis Reek
Elizabeth Suszynski
Completion Date: Immediate

Finding 3. The office did not adequately segregate duties related to processing payroll.

The office will establish a procedure under which OAH's Administrative Officer, Susan Schleisman, will review the payroll certification report. Ms. Schleisman will review all transactions and will initial and date the report upon the completion of the review and such additional control will alleviate risk.

Persons Responsible: Susan Schleisman
Dennis Reek
Completion Date: Immediate

Finding 4. The office did not comply with the state's special expense policy.

The office will update and revise its special expense plan and associated procedures and submit them to the Department of Employee Relations for approval. In addition, the office will develop an internal process and procedure wherein approvals are received in writing for all spending within the approved plan.

Person Responsible: Susan Schleisman
Dennis Reek
Completion Date: August 1, 2001

Sincerely,

/s/ Kenneth A. Nickolai

KENNETH A. NICKOLAI
Chief Administrative Law Judge

Telephone: 612/341-7640

KN:sh