



OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

Financial-Related Audit

Minnesota Tax Court
Three Fiscal Years Ended 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.

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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 H. Rest, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

The Honorable George W. Perez, Chief Judge
Minnesota Tax Court

We have audited the Minnesota Tax Court for the period July 1, 1997, through June 30, 2000, as further explained in Chapter 1. Our audit scope included payroll, administrative expenditures, and receipts. The following Summary highlights the audit objectives and conclusions. We discuss these issues more fully in the individual chapters of this report.

We conducted our audit in accordance with *Government Auditing Standards*, as issued by the Comptroller General of the United States. Those standards require that we obtain an understanding of management controls relevant to the audit. The standards also require that we design the audit to provide reasonable assurance that the Minnesota Tax Court complied with the provisions of laws, regulations, and contracts that are significant to the audit. Management of the court is responsible for establishing and maintaining the internal control structure and for compliance with applicable laws, regulations, and contracts.

We prepared this report for the information of the Legislative Audit Commission and the management of the Minnesota Tax Court. This restriction is not intended to limit the distribution of this report, which was released as a public document on August 16, 2001.

/s/ James R. Nobles

James R. Nobles
Legislative Auditor

/s/ Claudia J. Gudvangen

Claudia J. Gudvangen, CPA
Deputy Legislative Auditor

End of Fieldwork: April 6, 2001

Report Signed On: August 10, 2001

Minnesota Tax Court

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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
Cecile Ferkul, CPA, CISA	Audit Manager
Ellen Sibley	Auditor

Exit Conference

The following staff from the Minnesota Tax Court participated in the exit conference held on July 25, 2001:

George Perez	Chief Judge
Sheldyn Himle	Court Administrator

Report Summary

Key Findings:

- The Tax Court did not comply with state purchasing policies and legal provisions to obtain professional/technical services. The court used consultants who had master contracts with the state, but did not follow master contract procedures to procure the services. We recommended that the Tax Court work with the Department of Administration when procuring professional/ technical services. (Finding 1, page 7)
- The Tax Court did not review and approve invoices prior to payment. We recommended that the court document management or supervisory approval prior to processing payments. (Finding 2, page 8)
- The Tax Court did not follow certain provisions of the state's travel policy. The court did not properly document its travel reimbursement decisions and authorizations. We recommended that the Tax Court sufficiently document employee expense reimbursements and travel decisions to demonstrate that it has complied with state policies. (Finding 3, page 9)
- The Tax Court did not accurately account for its fixed assets. The Tax Court's inventory included items that it had disposed of in 1999. We recommended that the court maintain its fixed asset inventory list by recording additions and deletions as they occur. (Finding 4, page 10)

Agency Background:

Established in 1977, the Minnesota Tax Court is an executive branch court with statewide jurisdiction to hear and determine all matters arising out of Minnesota's tax laws. The Tax Court's mission is to provide timely and equitable disposition of appeals of orders issued by the commissioner of Revenue and local property tax determinations.

Financial-Related Audit Reports address internal control weaknesses and noncompliance issues found during our audits of state departments and agencies. The scope of our audit work at the Tax Court included payroll, rent, professional/technical services, supplies, equipment, travel, and receipts from July 1, 1997, through June 30, 2000. The Tax Court's response to our recommendations is included in this report.

Chapter 1. Introduction

In 1977 the Minnesota Legislature established the Minnesota Tax Court as a full-time court of record. The Tax Court is a specialized court in the executive branch with statewide jurisdiction to hear and determine all matters arising out of Minnesota's tax laws. The Governor appoints and the state Senate approves the appointment of each Tax Court judge. The judges serve six-year terms; there is no limit on their reappointment. There are three judges serving on the Tax Court. The three judges are responsible for designating a chief judge. Diane Kroupa served as chief from April 1998 through December 2000. George W. Perez, a member of the Tax Court since November 1997, became chief judge in January 2001.

The Tax Court's mission is to provide timely and equitable disposition of appeals of orders issued by the commissioner of Revenue and local property tax determinations including valuations, classifications, equalizations, or exemptions. It docket, tracks, schedules, and disposes of all cases filed. The court schedules and disposes of most appeals within one year of filing.

The Tax Court is responsible for complying with state statutes, policies, and procedures that are applicable to other executive branch agencies. These provisions include the state policies and procedures for purchases of goods, professional and technical services, travel reimbursements, and fixed assets, in addition to the following bargaining unit agreements:

- The Managerial Plan,
- The Middle Management Association, and
- The American Federation of State, County and Municipal Employee.

General Fund appropriations finance the Tax Court's operations. Table 1-1 shows the Tax Court's financial activity for the audit period.

Minnesota Tax Court

Table 1-1
Sources and Uses of Funds
For the Three Fiscal Years ended June 30, 2000

	<u>1998</u>	<u>1999</u>	<u>2000</u>
Sources:			
State Appropriations	\$974,000	\$ 645,000	\$660,000
Less: Cancellations	0	(8,119)	0
Transfers In ⁽¹⁾	0	112,000	57,540
Balance Forward In	0	349,717	0
Total Sources	<u>\$974,000</u>	<u>\$1,098,598</u>	<u>\$717,540</u>
Uses:			
Payroll ⁽²⁾	\$435,536	\$ 449,496	\$496,987
Rent	128,831	129,864	134,044
Professional/Technical Services ⁽³⁾	27,597	335,908	12,652
Travel	3,786	6,174	5,166
Supplies ⁽³⁾	9,394	22,963	6,476
Equipment	4,782	93,494	4,813
Other	14,357	30,975	10,296
Total Uses	<u>\$624,283</u>	<u>\$1,068,874</u>	<u>\$670,434</u>
Balance Forward Out to Next Fiscal Year	<u>\$349,717</u>	<u>\$ 0</u>	<u>\$ 47,106</u>
Unspent Appropriations⁽⁴⁾	<u>\$ 0</u>	<u>\$ 29,724</u>	<u>\$ 0</u>

- 1) The Tax Court received transfers from the Department of Administration in fiscal year 1999 for year 2000 conversion projects and in fiscal year 2000 to upgrade its computer network systems and software.
- 2) Payroll costs in fiscal year 2000 included the settlement of an employee grievance.
- 3) As noted in Finding 1, in fiscal year 1999, the Tax Court miscoded \$108,316 as Supplies rather than Professional/Technical Services. For Table 1-1, we adjusted the accounting system's data to properly classify expenditure transactions.
- 4) At April 30, 2001, the Tax Court had an encumbrance of \$29,724 remaining from its year 2000 conversion project. The Tax Court should continue to work with the Department of Finance to unencumber these funds.

Source: Minnesota Accounting and Procurement System (MAPS).

Chapter 2. Financial Activities

Chapter Conclusions

The Tax Court did not always follow state laws and policies when administering its financial activities. It did not properly obtain professional/technical services. It did not always properly authorize expenditure transactions. It did not comply with provisions of the state's travel policies. It did not accurately account for its fixed assets. Finally, the Tax Court did not promptly deposit receipts as required by statute.

Payroll

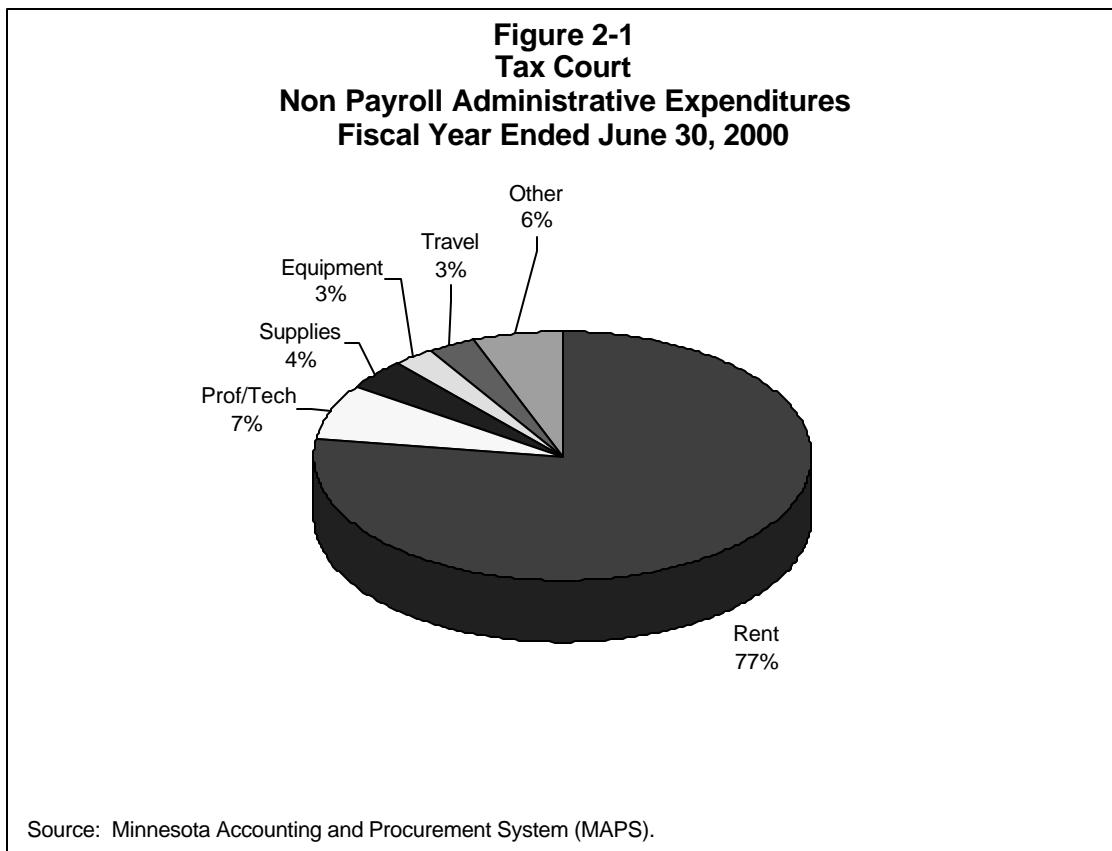
The Tax Court consists of three judges and three administrative staff positions. Since our last audit in fiscal year 1997, all employees in the judicial and administrative staff positions have changed.

Payroll expenditures accounted for approximately 58 percent of the Tax Court's expenditures. The Tax Court expended nearly \$500,000 in payroll related costs during fiscal year 2000. The Tax Court's employees were represented by three different bargaining agreements. In fiscal year 2000, the Tax Court's settlement of a grievance with an employee resulted in a payment of \$22,330. The Department of Employee Relations assisted the Tax Court with personnel actions and the Department of Finance assisted the court with payroll transaction processing.

Other Administrative Expenditures

The court's other administrative expenditures included rent for its office space in the state's Judicial Center in Saint Paul, professional/technical services to make significant upgrades in its case management system and its internal and external network connections, travel, equipment, and supplies. The Department of Finance's Small Agency Assistance unit helped the Tax Court to process its administrative expenditure transactions. Figure 2-1 shows the Tax Court's other administrative expenditures by type for the fiscal year ended June 30, 2000.

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Rent

The Tax Court leases office space on the second floor of the Judicial Building in the Capital Complex. For fiscal year 2000, expenditures for leased office space and parking totaled approximately \$134,000. The Department of Administration's Real Estate Management Division negotiated the Tax Court's lease for office space.

Professional/Technical Services

Professional/technical services accounted for approximately 12 percent of the Tax Court's expenditures. In fiscal years 1998 and 1999, the Department of Administration provided the Tax Court with \$112,000 for Year 2000 system upgrades and development. In fiscal year 2000, the Department of Administration/Office of Technology transferred to the Tax Court \$57,450 of the \$105,000 available for the Small Agency Infrastructure Initiative, which the Tax Court used primarily for development of the case management software and LAN administration, maintenance, and support. In fiscal year 2000, the Tax Court expended \$12,652 for professional/technical services. Finding 1 explains that the Tax Court did not properly procure professional/technical services. Also, as noted in Finding 1, the Tax Court miscoded some professional/technical services as supplies.

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Travel

The Tax Court incurred travel costs for the judges and the staff throughout the audit period. Fiscal year 2000 travel costs totaled \$5,166. The Tax Court hears commissioner of Revenue appeals in Ramsey County or will travel to the county in which the taxpayer resides. Members also travel to hear property tax cases in the county where the property is located. The members and staff were eligible for reimbursement of travel costs, including meals, lodging, private car mileage, and certain other expenditures in the amounts allowed in the bargaining unit agreements. As noted in Finding 3, the Tax Court did not always adequately support travel expenditures.

Supplies and Equipment

The Tax Court incurred \$11,289 in supply and equipment expenditures in fiscal year 2000. The majority of these expenditures were for the purchase of computer hardware and software to assist the staff in using the Tax Court's new computerized case management system, which began operation in the fall of 1998. As noted in Finding 1, the Tax Court miscoded some professional/technical services as supplies. Finding 4 explains that the court also did not maintain an accurate fixed asset inventory list.

Receipts

The Tax Court generated revenue through the collection of various filing fees. The Tax Court charged a \$122 fee for claims filed under its regular division as specified in Minn. Stat. Section 357.021, subd. 2, (1). For small claims cases that generally involved personal property or other small dollar amounts, the Tax Court charged a fee of \$25. Receipts from filing fees were approximately \$17,000, \$8,000, and \$9,000 for fiscal years 1998, 1999, and 2000, respectively. These fees are deposited to the General Fund as non-dedicated revenue. As explained in Finding 5, the Tax Court did not always promptly deposit these receipts.

Audit Objectives and Methodology

Our audit of payroll and other administrative expenditures focused on the following objectives:

- Did the Tax Court accurately report payroll and other administrative expenditures in the accounting records?
- Did the Tax Court comply with applicable finance-related legal provisions and management's authorization?

Our objective for the audit of receipts was to determine:

- Did the Tax Court safeguard and deposit receipts in accordance with applicable legal provisions?

Minnesota Tax Court

To answer these questions, we obtained an understanding of the internal control structure over payroll, rent, professional/technical services, travel, supplies, equipment, and receipts. We analyzed employee compensation and tested hours worked, pay rate increases, and travel reimbursements to ensure compliance with the terms of the applicable bargaining unit agreements. For supplies and equipment purchases and for professional/technical services, we analyzed and tested transactions to determine whether the purchases complied with the applicable Department of Administration's policies and procedures and whether payments were properly documented and authorized by management. We also tested the timeliness of receipt deposits.

Conclusions

The Tax Court did not always follow state laws and policies when administering its financial activities. As explained in Finding 1, it did not properly obtain professional/technical services. Finding 2 discusses how the Tax Court did not always authorize certain expenditures in the accounting system. Finding 3 discusses the court's noncompliance with certain provisions of the state's travel policies. Finding 4 shows that the court did not accurately account for its fixed assets. Finally, as explained in Finding 5, the Tax Court did not promptly deposit receipts as required by statute.

1. The Tax Court did not comply with state policies when it obtained some professional/technical services.

The Tax Court hired three consultants to assist it in developing a case management system that would be Year 2000 compliant and to establish an office network and web site. The Tax Court received \$112,000 through the Department of Administration for the Year 2000 compliance project, and \$105,000 for small agency infrastructure assistance. The consultants were:

- One consultant acted as the project coordinator to oversee the acquisition and implementation phases of the case management system and the installation of the court's internal and external networks. As explained below, the Tax Court did not properly procure these services. Payments to this consultant totaled \$189,748.
- Another consultant provided the software for the case management system, which it customized to the Tax Court's specific needs. Payments to this consultant totaled \$108,316. The Department of Administration assisted the Tax Court with procuring these services. The Tax Court miscoded these expenditures as supplies on the state's accounting system. Without accurate expenditure coding, the Tax Court cannot rely on the accounting data to monitor spending.
- The Tax Court hired the third consultant to serve as the project risk manager to "provide an unbiased evaluation of the Tax Court's Systems Project to increase the likelihood of achieving the project's objectives." As explained below, the Tax Court did not properly procure these services. Payments to this consultant totaled \$33,602.

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The Tax Court improperly obtained the services of the project coordinator and the project risk manager through Master Contracts for professional/technical services. Although the court chose the consultants from the state's list of Master Contract vendors for professional/technical services, it did not follow the state's Master Contract procedures to procure those services. A Master Contract is a contract the state enters into with a vendor for certain services, although the state does not specifically know which agency or when the agency will need the services. To use a Master Contract vendor, a state agency completes a work order that includes a detailed Statement of Work. If the work order is for \$5,001 to \$99,999, the agency sends the statement of work to ten Master Contract vendors to obtain proposals and can then select the vendor that provides the best value. If the work order is for \$100,000 or greater, the agency needs to have the Office of Technology review and approve it prior to selecting a vendor to complete the work.

The Tax Court did not follow any of these procedures to obtain the professional/technical services. The Tax Court used purchase orders, instead of work orders, did not request proposals from other Master Contract vendors, and did not have the Office of Technology review and approve the proposed work. The state establishes policies and procedures for certain types of purchases and for transactions over a certain amount to ensure that the state obtains the best value for its money. It is especially important for a small agency to follow the proper process and involve the Department of Administration since it lacks expertise about the technical nature of the services and the contract process. The Office of Technology also may have suggested better project specifications to avoid the need for amendments to the scope of the project that added to its cost.

Recommendations

- *The Tax Court should work with the Department of Administration to ensure it makes purchases in accordance with state policy and applicable legal provisions.*
- *The Tax Court should ensure that it properly codes expenditures in the state's accounting system.*

2. The Tax Court did not review and approve invoices prior to payment.

The Tax Court's management or supervisory staff had not approved seven of the ten tested invoices totaling \$25,459. The Tax Court also could not locate documentation for a \$2,075 payment. The Tax Court's management or supervisory staff should review and approve invoices prior to payment to ensure that the transactions are accurate, properly authorized, adequately documented, and properly coded.

Recommendation

- *The Tax Court should document management or supervisory staff approval prior to processing payments.*

Minnesota Tax Court

3. PRIOR FINDING NOT RESOLVED: The Tax Court did not follow certain provisions of the state's travel policy.

The Tax Court did not always obtain documentation to support its travel reimbursement decisions and authorizations.

The Tax Court did not properly document the authorization for five out-of-state trip reimbursement requests totaling \$4,000. Although various documents supported the court's assertion that the chief judge approved the travel arrangements in advance, the court did not use the Department of Finance's "Authorization for Travel" form. The Department of Finance requires that executive branch agencies use this form to ensure that travel costs comply with policies and procedures of the Departments of Finance, Employee Relations, and Administration, and with labor agreements and compensation plans. The form should document an estimate of all costs, the name, location, and dates of the event, and the reason why the trip is necessary. The form should also detail any financial decisions made, such as weekend stays to obtain lower airfares or an analysis to support the reasonableness of other modes of transportation. The court did not always document the lowest airfare or justify the additional hotel and meal costs when extending a trip to obtain the lowest airfare.

Employee expense reports sometimes lacked certain information needed to demonstrate compliance with reimbursement requirements. For example:

- Expense reports did not always include a vehicle control number from the state's Travel Management division to document that a state vehicle was not available. State policies allow for the state to reimburse employees for use of their private vehicle at a higher rate if a state vehicle was not available. For four of the five mileage reimbursements we tested, the Tax Court either adjusted the expense report prior to payment or the employees repaid the difference between the higher and lower reimbursement rates.
- Some employee reimbursement claims lacked departure and arrival times to claim meals. The departure and arrival times determine when the employee was in travel status and thus eligible for meal reimbursements.
- Some employee expense reimbursement claims did not accurately distinguish between trip and local miles. In documenting miles driven, state policy requires employees to report trip and local miles separately.

The Tax Court lacked a process for ensuring that employee travel reimbursement requests complied with state policy. The state designed its employee expense reimbursement form to document the information needed to comply with state policy and bargaining unit agreements.

Recommendations

- *The Tax Court should document its decisions and authorizations for out-of-state travel, in accordance with state policies.*

Minnesota Tax Court

- *The Tax Court should follow state policy and procedures to ensure that employees are reimbursed only for allowable expenditures and at appropriate rates.*

4. The Tax Court did not accurately account for its fixed assets.

The Tax Court did not maintain accurate fixed asset records. In March 1999, the Tax Court disposed of seven items, totaling \$19,512, without deleting them from the fixed asset list. One of these items was a computer purchased for \$13,400. The Tax Court identified these errors when it conducted a physical inventory during the audit. The Department of Administration's Materials Management Division requires that agencies maintain an accurate fixed asset inventory list for assets that exceed \$2,000.

Recommendation

- *The Tax Court should maintain its fixed asset inventory list by recording additions and deletions to the inventory as they occur.*

5. The Tax Court did not deposit all receipts in excess of \$250 daily.

The Tax Court did not always deposit receipts daily as required by state law. Tax Court staff were not aware of the statutory provision. Minn. Stat. Section 16A.275 requires that the Tax Court deposit all receipts in excess of \$250 daily. The Tax Court collects a \$122 fee for claims filed under its regular division and \$25 for small claim cases. The Tax Court generally deposited receipts one to three times each month. The number of checks in a deposit ranged from four to over thirty.

Recommendation

- *The Tax Court should deposit receipts promptly as required by Minn. Stat. Section 16A.275.*

Status of Prior Audit Issues As of April 6, 2001

Most Recent Audit

Legislative Audit Report 98-22, issued in March 1998, covered the three fiscal years ended June 30, 1997. The scope of this audit included payroll, rent, professional development, travel, and communications. The report included one written issue related to travel. Although the court implemented changes in their travel reimbursement practices, problems persisted. See current Finding 3.

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 the metropolitan agencies, or the State Agricultural Society, the state constitutional officers, or the judicial branch.



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August 9, 2001

Mr. James Nobles
Legislative Auditor
Centennial Building

Dear Mr. Nobles:

We have received and reviewed the audit report for the period of July 1, 1997 to June 30, 2000. In response to the key findings, we have taken the following actions to implement your recommendations:

Two of three Court staff have been certified as having Authority for Local Purchase (ALP), one in April and another in July of 2001, (although only one is required). We are working closely with the Department of Administration to ensure adherence to state policies and statutory requirements.

Court staff is working closely with MAPS Small Agency assistance personnel to ensure proper coding of expenditures.

ALP guidelines are being followed when making purchasing decisions. Review and approval occurs before making payment, noting the date and person giving approval on the invoice.

The Tax Court will utilize the Department of Finance's Authorization Travel form to document authorized out-of-state travel. Tax Court expenses submitted for reimbursement will have supporting documentation indicating appropriate rates of reimbursement allowable.

The fixed asset inventory list will be updated when additions or deletions occur.

The Tax Court is depositing funds when it collects \$250 as required by statute.

Sincerely,

/s/ George W. Perez

George W. Perez, Chief Judge

cc: Judge Krause
Judge Sanberg
Sheldyn Himle, Court Administrator

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