



**OFFICE OF THE LEGISLATIVE AUDITOR**  
STATE OF MINNESOTA

Financial-Related Audit

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# **Office of the State Auditor**

## **January 1, 2001, through December 31, 2002**



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## 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.

All findings, conclusions, and recommendations in reports issued by the Office of the Legislative Auditor are solely the responsibility of the office and may not reflect the views of the LAC, its individual members, or other members of the Minnesota Legislature.

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All OLA reports are available at our Web Site: <http://www.auditor.leg.state.mn.us>

If you have comments about our work, or you want to suggest an audit, investigation, evaluation, or best practices review, please contact us at 651-296-4708 or by e-mail at [auditor@state.mn.us](mailto:auditor@state.mn.us)



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

Representative Tim Wilkin, Chair  
Legislative Audit Commission

Members of the Legislative Audit Commission

The Honorable Patricia Awada  
State Auditor

We have audited the Office of the State Auditor for the period January 1, 2001, through December 31, 2002. Our audit scope included appropriation control, audit practice receipts, payroll, and other administrative expenditures. The audit objectives and conclusions are highlighted 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 require that we design the audit to provide reasonable assurance that the Office of the State Auditor complied with provisions of laws, regulations, contracts, and grants that are significant to the audit. The management of the Office of the State Auditor is responsible for establishing and maintaining the internal control structure and complying with applicable laws, regulations, contracts, and grants.

This report is intended for the information of the Legislative Audit Commission and the management of the Office of the State Auditor. This restriction is not intended to limit the distribution of this report, which was released as a public document on May 2, 2003.

/s/ James R. Nobles

James R. Nobles  
Legislative Auditor

/s/ Claudia J. Gudvangen

Claudia J. Gudvangen, CPA  
Deputy Legislative Auditor

End of Fieldwork: February 28, 2003

Report Signed On: April 29, 2003

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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
Jim Riebe, CPA	Audit Manager
Joan Haskin, CPA, CISA	Auditor-in-Charge
Gena Hoffman	Auditor

### **Exit Conference**

We discussed the results of the audit with the following staff of the Office of the State Auditor at an exit conference on April 22, 2003:

Pat Awada	State Auditor
Greg Hierlinger	Deputy State Auditor, Audit Practice
Matt Lindemann	Assistant State Auditor, Director of Budget, Finance, and Technology

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## Report Summary

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### Audit Conclusions:

The Office of the State Auditor (OSA) spent its state appropriation within its established authority. The office's internal controls provided reasonable assurance that assets were safeguarded and financial activities were properly recorded in the state's accounting system. Except for the finding below, the office complied with applicable legal provisions for items tested.

### Finding:

- The OSA did not recover its audit practice costs in fiscal years 2001 and 2002, as required by Minn. Stat. Section 6.58. OSA audit practice expenditures exceeded audit receipts by \$344,000 in 2001 and \$229,000 in 2002. The office budgeted to under-recover costs by approximately \$736,000 in fiscal year 2003. Minnesota statutes require the office to annually recover its audit practice costs. The auditor's practice, which was approved by the Department of Finance, has been to use prior years' over-recoveries to offset current year under-recoveries. We recommended that the OSA set its billable rates at a level sufficient to recover audit practice costs as required by statute, or seek statutory authority for its current practice of offsetting prior years' over-recoveries of costs. (Finding 1, page 8)

### Agency Background:

The OSA was established by Article V of the State Constitution and operates under Minnesota Statute Chapter 6. Minnesota voters elect the state auditor to a four-year term. Judith Dutcher was state auditor from January 1995 through December 2002. Patricia Awada was elected state auditor in November 2002 and began her term on January 6, 2003. The mission of the OSA is to help ensure financial integrity, accountability, and cost-effectiveness in over 4,300 governmental entities throughout the state. The state auditor serves on the State Executive Council, State Board of Investment, Land Exchange Board, Minnesota State Housing Finance Agency Board, Public Employees Retirement Association Board, and Rural Finance Authority Board.

The OSA's operations are funded by state appropriations. The office's appropriation in fiscal year 2002 totaled approximately \$10 million. The audit practice receipts collected from local units of government are deposited in the General Fund as non-dedicated receipts.

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## Chapter 1. Introduction

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The Office of the State Auditor (OSA) was established by Article V of the State Constitution and operates under Minn. Stat. Chapter 6. Minnesota voters elect the state auditor to a four-year term. Judith Dutcher was state auditor from January 1995 through December 2002. Patricia Awada is the current state auditor. She began her term on January 6, 2003. The state auditor serves on the State Executive Council, State Board of Investment, Land Exchange Board, Minnesota State Housing Finance Agency Board, Public Employees Retirement Association Board, and Rural Finance Authority Board.

The OSA is divided into six divisions:

- The Constitutional Office Division oversees the operation of the Office of the State Auditor.
- The Audit Practice Division conducts financial and legal compliance audits for 87 counties; the cities of Duluth, Minneapolis, and St. Paul; and organizations affiliated with counties and cities. In addition, this division annually reviews approximately 450 single audit reports submitted by cities, counties, school districts, nonprofit agencies, and other agencies for compliance with federal requirements and generally accepted government auditing standards.
- The Government Information Division promotes financial accountability and cost effective public services in local governments. The division prescribes the chart of accounts and reporting requirements for cities and towns.
- The Special Investigations Division promotes integrity and accountability in local government by investigating allegations of financial wrongdoing.
- The Pension Division monitors investment, financial, and actuarial reporting for public pension funds to ensure financially stable retirement systems and compliance with Minnesota statutes governing these activities.
- The Tax Increment Financing Division audits and monitors the financial condition and legal compliance of tax increment financing districts throughout the state. The division collects and analyzes financial information that local governments are required to report annually regarding their use of tax increment financing.

The OSA's activities are financed primarily through General Fund appropriations. The OSA's appropriations after budget reductions for fiscal years 2001, 2002, and 2003 were \$9.3 million, \$9.5 million, and \$9.8 million, respectively. We discuss appropriations more fully in Chapter 2.

## Office of the State Auditor

Minn. Stat. Section 6.58 requires that the OSA collect fees from audited organizations to cover its audit costs. The Audit Practices Division bills the political subdivisions it audits based on a fee schedule that OSA adjusts annually if necessary. According to Minn. Stat. Section 16A.6701, the fees collected for audit services are deposited in the General Fund. We discuss the audit practice revenue in Chapter 3.

The OSA incurs administrative costs in carrying out its statutory responsibilities. Payroll is the most significant administrative cost. Other material costs include rent, supplies and equipment, and travel. We discuss OSA expenditures in Chapter 4.

Table 1-1 summarizes the financial activity of the OSA for fiscal year 2002.

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**Table 1-1**  
**Summary of OSA Financial Activity**  
**Fiscal Year 2002**

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Sources:	
General Fund:	
Operating Appropriation	\$10,051,000
Less Appropriation Reduction	<u>(503,000)</u>
Net Appropriation	\$ 9,548,000
Transfer In – TIF Account <sup>(1)</sup>	823,115
Balance Forward In – TIF Account <sup>(1)</sup>	234,518
Special Revenue Fund:	
Dedicated Revenue <sup>(2)</sup>	23,900
Balance Forward In	<u>306</u>
Total Sources	<u>\$10,629,839</u>
Uses:	
Expenditures:	
Payroll	\$ 8,782,450
Rent	396,407
Travel, In and Out State	147,935
Supplies	92,843
Capital Equipment	33,356
Miscellaneous Expenditures	<u>247,877</u>
Total Expenditures	<u>\$ 9,700,888</u>
Other Uses:	
Balance Forward Out – General Fund	\$ 925,088
Balance Forward Out – Special Revenue Fund	1,803
Transfer Out	<u>2,060</u>
Total Other Uses	<u>\$ 928,951</u>
Total Uses	<u>\$10,629,839</u>

Notes:

- (1) Minn. Stat. Section 469.177, Subd. 11 created the TIF division. The division received funding from a .25 percent charge on TIF districts in fiscal year 2002. The Office of the State Treasurer collected the funds, deposited the money in the General Fund, and then transferred the funds to the OSA.
- (2) Dedicated revenue is collected for seminar and workshop activities.

Source: Minnesota Accounting and Procurement System.

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## Chapter 2. Appropriation Control

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### *Chapter Conclusions*

*The OSA complied with appropriation laws and operated within its legally authorized funding level. Expenditures were recorded properly on the state's accounting system. Residual funds were canceled or carried forward as required by law.*

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### Background

The OSA received funding for its operations through a General Fund appropriation. The OSA allocated the appropriation to five operating divisions. Table 2-1 summarizes financial activity for these divisions for fiscal year 2002.

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**Table 2-1**  
**Summary of General Fund Appropriation Allocation**  
**Fiscal Year 2002**

<u>Division</u>	<u>Appropriation</u>	<u>Amount Expended</u>	<u>Balance Forward to FY 2003</u>
Audit Practice	\$7,401,550	\$6,886,156	\$515,394
Government Information	633,250	577,080	56,170
Special Investigations	572,000	561,565	10,435
Constitutional Office	368,150	362,846	5,304
Pension	<u>573,050</u>	<u>505,890</u>	<u>67,160</u>
Total Appropriation (after budget reduction)	<u>\$9,548,000</u>	<u>\$8,893,37</u>	<u>\$654,463</u>

Source: Minnesota Accounting and Procurement System.

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The portion of the OSA appropriation that is spent on oversight of police and fire pension funds and the government information function reduces police and fire state aid and local government aid administered by the Department of Revenue. The OSA certifies costs related to the government information function to the Department of Revenue for a reduction in local government aids as specified in Minn. Stat. Section 477A.014, Subd. 4. The local government aid offset is limited to \$217,000 per year. The OSA also certifies costs related to the Pension Division to the Department of Revenue in accordance with Minn. Stat. Section 69.021, Subd. 5. The Department of Revenue reduces police and fire state aids by the amount of OSA costs associated with the audits or exams of the police and firefighters relief associations. For fiscal year 2002, the OSA certified projected costs for firefighter and police relief aid associations of \$319,880 and \$2,256, respectively.

## **Office of the State Auditor**

In addition to the General Fund appropriation, the OSA receives funding for the cost of examining the use of tax increment financing (TIF). Minn. Stat. Section 469.177, Subd. 11 provided that the TIF division received funding from a .25 percent charge on tax increment financing districts during the audit period. The Treasury Division of the Department of Finance collects the funds from the county treasurers, deposits the money in the General Fund, and subsequently transfers the funds to the OSA. TIF revenue collections in fiscal year 2002 totaled \$823,115. Total TIF division expenditures in fiscal year 2002 were approximately \$787,000. The division carried forward about \$271,000 to fiscal year 2003.

### **Audit Objectives and Methodology**

Our audit of OSA appropriations addressed the following questions:

- Did the office comply with appropriation laws?
- Were expenditures properly recorded in the accounting system?
- Were residual funds canceled, carried over, or transferred as required by law?

To answer these questions, we reviewed appropriation laws and accounting system summary information and supporting documentation. We discussed appropriation activity with OSA personnel. We also used computer software to analyze financial data.

### **Conclusions**

The OSA complied with the provisions of the appropriation laws and operated within its legally authorized funding level. Expenditures were properly recorded in the accounting system. Residual funds were administered in the proper manner required by law.

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## Chapter 3. Audit Practice Revenue

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### *Chapter Conclusions*

*The OSA's internal control structure provided reasonable assurance that receipt transactions were billed at the approved rate and accurately recorded in the accounting records. The office adequately safeguarded audit practice receipts. The OSA complied with material finance-related legal provisions regarding receipts, except that in fiscal years 2001 and 2002 the OSA did not establish charges for audit examinations at a level sufficient to recover audit costs as required by Minn. Stat. Section 6.58.*

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### **Background**

The OSA conducts financial and compliance audits of local governments in Minnesota. The OSA bills local governments for associated audit costs. The OSA deposits audit practice receipts into the General Fund. These receipts are not available for expenditure by the OSA, as its spending is limited to the appropriation authority discussed in Chapter 2.

Minn. Stat. Section 6.58 requires OSA to review and adjust the schedule of charges for audit examinations at least annually to ensure that the amount collected is sufficient to pay all costs connected with such examinations. The Department of Finance approved rate increases of four percent each for calendar years 2001, 2002, and 2003.

For fiscal year 2002, the OSA collected approximately \$6.4 million in audit practice receipts coded to budget fiscal year 2002. The OSA bills audit clients for completed audits on a monthly basis. The basis for billing a client includes approved audit charges and travel costs. The OSA has the authority to charge interest on delinquent accounts of undisputed bills that are 60 days past due.

### **Audit Objective and Methodology**

The primary objective of our review of audit practice revenues was to answer the following questions:

- Did the office's internal control structure provide reasonable assurance that receipt transactions were billed at the proper rate and accurately reported in the accounting records?
- Were audit practice receipts adequately safeguarded?

## Office of the State Auditor

- Did the office comply with material finance-related legal provisions regarding receipts?

To answer these questions, we interviewed office employees to gain an understanding of the internal control structure over the billing and collection process. We tested the client billing and accounts receivable process to determine whether billed amounts were substantiated. We also analyzed audit practice revenue transactions and supporting documentation for proper authorization, recording, collection, and deposit of client payments pursuant to Minnesota statutes. Finally, we performed a cost recovery analysis to assess whether the OSA recovered its costs for the audit examinations it conducts.

### Conclusions

The OSA's internal control structure provided reasonable assurance that receipt transactions were billed at the approved rate and accurately reported in the accounting records. Audit practice receipts were adequately safeguarded. The OSA complied with material finance-related legal provisions regarding receipts, except that as noted in Finding 1, the OSA has not generated sufficient revenues to recover reimbursable audit costs, as required by Minn. Stat. Section 6.58, since fiscal year 2000.

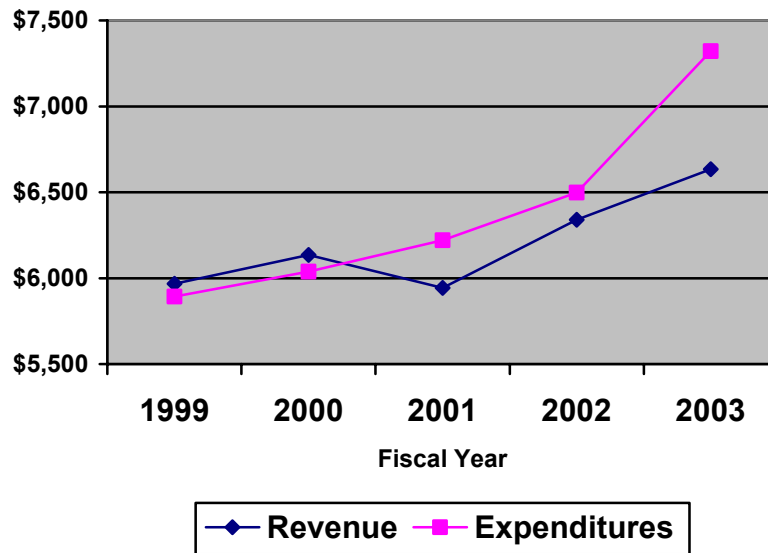
#### **1. The OSA did not recover its audit costs as required by Minn. Stat. Section 6.58.**

Audit practice receipts for fiscal years 2001 and 2002 were not sufficient to recover all costs of OSA examinations. OSA audit expenditures exceeded audit receipts by \$344,000 in 2001 and \$229,000 in 2002. The office budgeted to under-recover costs for 2003 by \$736,000. According to OSA staff, the office budgeted to under-recover its costs in order to offset prior years over-recoveries of costs. The over-recoveries occurred as long ago as fiscal year 1994. As of fiscal year 2002, the balance totaled about \$1.4 million.

Minn. Stat. Section 6.58 states that the OSA shall set its schedule of charges for examinations at least annually to ensure that the amount collected is sufficient to pay all costs connected with the examinations during the fiscal year. The Department of Finance (DOF) approved rate increases of four percent each for the calendar years 2001 and 2002. DOF did not initially approve the 2003 rate schedule because revenues would fall short of projected expenditures. However, in December 2002, DOF approved a four percent rate increase but was still concerned that the rates were not in compliance with Minnesota Statute Section 6.58.

The budgeted revenues and expenditures in Figure 3-1 shows the OSA did not sufficiently increase charges to recover audit costs.

**Figure 3-1**  
**Audit Practice Revenue and Expenditures**  
**By Fiscal Year**  
**(in thousands)**



Note: The graph shows budgeted numbers for fiscal year 2003.

Source: OSA analysis of audit practice revenues and expenditures.

*Recommendation*

- *The OSA should set its billable rates at a level sufficient to recover audit practice costs as required by Minn. Stat. Section 6.58, or seek statutory authority for its current practice of offsetting prior years' over-recoveries of costs.*

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## Chapter 4. Payroll and Other Administrative Expenditures

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### *Chapter Conclusions*

*The OSA's internal control structure provided reasonable assurance that payroll and other administrative expenditure transactions were proper and accurately recorded in the accounting records. The OSA complied with applicable finance-related legal provisions and bargaining unit agreements for items tested.*

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### Background

The OSA incurs administrative expenditures for personnel services, travel, supplies and equipment, rent, and other miscellaneous expenses. Personnel services represented approximately 90 percent of total expenditures. Travel, rent, and supplies and equipment represented the majority of other administrative expenditures. We discuss payroll and other administrative expenditures in the following sections.

### Payroll

The OSA employs about 130 staff located in offices throughout the state. The employees are covered by various bargaining unit agreements. The OSA administers a separate personnel plan for those employees not covered by the bargaining unit agreements. Table 4-1 highlights the types of payroll expenditures for fiscal year 2002.

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**Table 4-1**  
**Payroll Expenditures**  
**Budget Fiscal Year 2002**

<u>Payroll Type</u>	<u>Amount</u>
Full-time Salaries	\$8,459,250
Part-time Salaries	110,469
Overtime	72,962
Severance/Vacation Payoffs/Other	<u>139,767</u>
Total Payroll	<u>\$8,782,448</u>

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Sources: OLA summary of expenditures for budget fiscal year 2002 through December 31, 2002.

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Bi-weekly payroll transactions and pay rate changes are processed through the Department of Employee Relations' State Employee Management System (SEMA4). These transactions are

## **Office of the State Auditor**

also recorded in the Minnesota Accounting and Procurement System (MAPS) through a computer system interface.

### **Audit Objective and Methodology**

The primary objective of our audit of payroll was to answer the following questions:

- Did the office's internal control structure provide reasonable assurance that payroll expenditure transactions were accurately reported in the accounting records?
- Were employees paid in accordance with material finance-related legal provisions, including state bargaining unit agreements?

The methodology we used to meet these objectives included inquiries of staff and analytical procedures. We reviewed bargaining unit agreements and interviewed key department employees to gain an understanding of the internal control structure over payroll and personnel functions. In addition, we analyzed a sample of transactions for legal compliance provisions, propriety of transactions, and proper recording in the accounting system.

### **Conclusions**

The office's internal control structure provided reasonable assurance that payroll expenditure transactions were accurately reported in the accounting records. For the items tested, employees were paid in accordance with material finance-related provisions, including state bargaining unit agreements.

### **Other Administrative Expenditures**

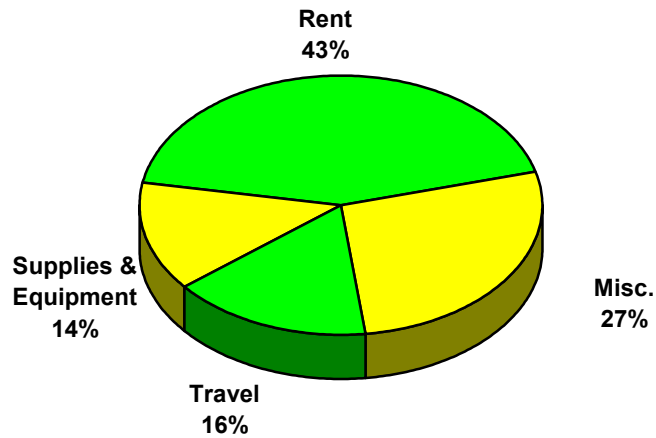
Other administrative expenditures accounted for approximately nine percent of total operating costs. The OSA incurred administrative expenditures in the following categories: rent, travel, and supplies and equipment, as well as other miscellaneous areas.

The largest non-payroll expenditure is for the lease of office space. The Real Estate Management Division of the Department of Administration assists the OSA in negotiating lease agreements. The OSA is currently leasing office space for employees in St. Paul and other locations throughout the state. In fiscal year 2002, the office paid approximately \$390,000 for office and storage space at 12 locations.

Figure 4-1 illustrates the fiscal year 2002 non-payroll administrative expenditures by type. The miscellaneous category is comprised mainly of professional/technical services, purchased services, and communication expenses.



**Figure 4-1  
Non-payroll Administrative Expenditures  
Fiscal Year 2002**



Source: OLA summary of expenditures for budget fiscal year 2002 through December 31, 2002.

## **Audit Objective and Methodology**

The primary objective of our audit of rent, travel, and supplies and equipment expenditures was to answer the following questions:

- Did the office's internal control structure provide reasonable assurance that administrative expenditure transactions were accurately reported in the accounting records and in accordance with management's authorization?
- Did the office comply with material finance-related legal provisions?

To address these objectives, we interviewed agency staff to gain an understanding of the space rental, purchasing, and payment processes. We selected a sample of expenditures and verified that they were approved and properly recorded in the accounting system.

## **Conclusions**

The office's internal control structure provided reasonable assurance that administrative expenditure transactions were accurately reported in the accounting records and in accordance with management's authorization. For the items tested, the OSA complied with material finance-related legal provisions.

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## Status of Prior Audit Issues As of February 28, 2003

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**May 2001, Legislative Audit Report 01-29** covered the two years ended December 31, 2000. The scope of the audit included appropriation control, audit practice revenues, personnel services, and other administrative expenditures. There were no findings or recommendations that resulted from the audit.

### 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.

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PATRICIA AWADA  
STATE AUDITOR

## STATE OF MINNESOTA OFFICE OF THE STATE AUDITOR

SUITE 400  
525 PARK STREET  
SAINT PAUL, MN 55103-2139

(651) 296-2551 (Voice)  
(651) 296-4755 (Fax)  
stateauditor@osa.state.mn.us (E-mail)  
1-800-627-3529 (Relay Service)

April 21, 2003

Mr. James R. Nobles, Legislative Auditor  
Office of the Legislative Auditor  
Room 140 Centennial Building  
658 Cedar Street  
St. Paul, Minnesota 55155

Dear Mr. Nobles:

Thank you for the opportunity to respond to the finding in the financial and compliance audit of the Office of the State Auditor (OSA) for the two years ended December 31, 2002. The following is our response to the April 11, 2003 draft audit report.

**Audit Finding: The OSA did not recover its audit costs as required by Minn. Stat. Section 6.58.**

The OSA agrees with the audit finding. Beginning with the fiscal year ending June 30, 2004, the OSA will generate sufficient revenues to recover the cost of conducting audits. The OSA will review projected costs and revenues for the fiscal year ending June 30, 2004, and request an increase in hourly rates from the Department of Finance. The new rates will be effective on January 1, 2004.

If additional information is required feel free to contact me or my office.

Sincerely,

*/s/ Pat Awada*

Patricia Awada  
State Auditor

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**VIA FACSIMILE**

April 28, 2003

Mr. Jim Nobles  
Legislative Auditor  
Room 140 Centennial Building  
658 Cedar Street  
St. Paul, Minnesota 55155-1603

Dear Mr. Nobles:

Please find enclosed a copy of my response to the Legislative Auditor's audit of the Office of the State Auditor, for January 2001 to December 2002. The enclosed comment is in response to the finding contained in *Chapter 3. Audit Practice Revenue; 1. The OSA did not recover its audit costs as required by Minn. Stat. Section 6.58*. I have not conferred with State Auditor Awada regarding this response but I am forwarding a copy to Mr. Greg Hierlinger of the State Auditor's office for his records.

If you would like to contact me directly, I can be reached at my new job as President of the Minnesota Community Foundation, (651) 325-4213.

I want to thank you for the good work and professionalism of your staff. I wish you every success in the future.

Sincerely,

*/s/ Judi Dutcher*

Judi Dutcher

JUDI DUTCHER, STATE AUDITOR JAN. 1995 THROUGH JAN. 2003,  
RESPONSE TO THE LEGISLATIVE AUDITOR'S REPORT  
APRIL 28, 2003

CHAPTER 3 AUDIT PRACTICE REVENUE

COMMENT 1. The OSA did not recover its audit costs as required by Minn. Stat. Section 6.58.

RESPONSE: The OSA respectfully disagrees with the Legislative Auditors' interpretation of the law. The OSA has, in fact, recovered its audit costs as required by Minn. Stat. § 6.58. This law requires the State Auditor "to adjust the schedule of charges for such examinations to provide that such charges shall be sufficient to cover all costs of such examinations and that the ***aggregate charges collected*** shall be sufficient to pay all salaries and other expenses . . . "(emphasis added)

The OSA is not allowed by law to make a profit; instead it is required by law to annually review and adjust its schedule of charges. The OSA's schedule of charges is submitted to the Department of Finance for approval on an annual basis. The rate schedule is examined to make certain that the funds collected will be *sufficient* to pay for the audit examinations and that the charges are *equitable*. The Legislative Auditor is now interpreting Minn. Stat. § 6.58 to require that revenues must be collected in one year to pay all the costs of that same year. The law does not require that the OSA recover the cost of its examinations in such a manner and the OSA's cost recovery methods have been consistently applied for the past 12 years.

Since FY 1991, the OSA has aggregated the collection of audit fees so that accumulated balances would be used to offset future expenditures. Likewise, if sufficient funds were not collected during the audit year, additional fees were imposed on the audit clients in subsequent years in order to recover costs. The principals of equity as set forth in Minn. Stat. § 6.58 requires not only that any shortfall in collected fees be made up by the OSA's local government audit clients, but also that any excess fees collected be refunded to these clients, instead of reverting to the state's general fund. If the practice of aggregating fees is to now change to allow the state to keep all surpluses collected, then equitably the state must contribute to all deficits that may arise.

The agreed upon application of the law was set forth in a letter dated August 25, 1997 from Minnesota State Auditor Judi Dutcher to Finance Commissioner Wayne Simoneau. This letter states "it has been the statutory interpretation of the Department of Finance that it would be contrary to legislative intent to charge clients a per diem rate, and subsequently not give them credit for these charges in the fund balance . . . The Department of Finance staff agreed that the OSA could use such funds from an accumulated balance forward to offset expenditures in the future biennium." Therefore,



the OSA has recovered its costs and set its rates in accordance with the law and has acted in reliance upon past practices.

It should be noted that in addition to the annual review and approval by the Department of Finance, the OSA's rate recovery method has been the subject of a biennial review and approval by the Minnesota Legislature through the biennial budget process. If the method and manner of cost recovery were to be changed, it would require an affirmative amendment to current law. Since 1991 every commissioner of Finance has signed-off on the OSA's rate recovery schedule and methodology. Therefore, the OSA respectfully disagrees with the Legislative Auditor's legal interpretation of Minn. Stat. §6.58.