

**OFFICE OF THE ATTORNEY GENERAL**

**FINANCIAL AUDIT**

**FOR THE TWO YEARS ENDED DECEMBER 31, 1992**

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**AUGUST 1993**

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Financial Audit Division  
Office of the Legislative Auditor  
State of Minnesota

**93-43**



**OFFICE OF THE ATTORNEY GENERAL**  
**FINANCIAL AUDIT**  
**FOR THE TWO YEARS ENDED DECEMBER 31, 1992**

Public Release Date: August 20, 1993

No. 93-43

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**OBJECTIVES:**

- **EVALUATE INTERNAL CONTROL STRUCTURE:** Billings for services, litigation settlement revenue, and payroll.
- **TEST COMPLIANCE WITH CERTAIN FINANCE-RELATED LEGAL PROVISIONS.**

**CONCLUSIONS:**

We found one area where the Office of the Attorney General's internal control structure needed improvement and it did not comply with finance-related legal provisions:

- The Office of the Attorney General has supplemented its appropriation authority by charging some attorneys' salaries directly to other state agencies.

Contact the Financial Audit Division for additional information.  
296-1730

FINANCIAL AUDIT DIVISION





STATE OF MINNESOTA

**OFFICE OF THE LEGISLATIVE AUDITOR**

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JAMES R. NOBLES, LEGISLATIVE AUDITOR

Senator Phil Riveness, Chairman  
Legislative Audit Commission

Members of the Legislative Audit Commission

The Honorable Hubert H. Humphrey, III  
Attorney General

## **Audit Scope**

We have conducted a financial related audit of the Office of the Attorney General as of and for the two years ended December 31, 1992. Our audit was limited to only that portion of the State of Minnesota's financial activities attributable to the transactions of the Office of the Attorney General, as discussed in the Introduction. We have also made a study and evaluation of the internal control structure of the Office of the Attorney General in effect at December 31, 1992.

We conducted our audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial activities attributable to the transaction of the Office of the Attorney General are free of material misstatements.

As part of our study and evaluation of the internal control structure, we performed tests of the Office of the Attorney General's compliance with certain provisions of laws, regulations, contracts, and grants. However, our objective was not to provide an opinion on overall compliance with such provisions.

## **Management Responsibilities**

The management of the Office of the Attorney General is responsible for establishing and maintaining an internal control structure. This responsibility includes compliance with applicable laws, regulations, contracts, and grants. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that:

- assets are safeguarded against loss from unauthorized use or disposition;
- transactions are executed in accordance with applicable legal and regulatory provisions, as well as management's authorization; and

- transactions are recorded properly on the statewide accounting system in accordance with Department of Finance policies and procedures.

Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

### **Internal Control Structure**

For purposes of this report, we have classified the significant internal control structure policies and procedures in the following categories:

- billings for services,
- litigation settlement revenue, and
- payroll.

For all of the internal control structure categories listed above, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk.

### **Conclusions**

Our study and evaluation disclosed the conditions discussed in finding #1 involving the internal control structure of the Office of the Attorney General. We consider this condition to be a reportable condition under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the entity's ability to record, process, summarize, and report financial data.

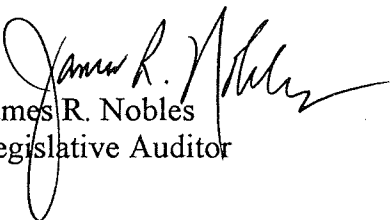
A material weakness is a reportable condition in which the design or operation of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial activities being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We do not believe the reportable condition described above is a material weakness.

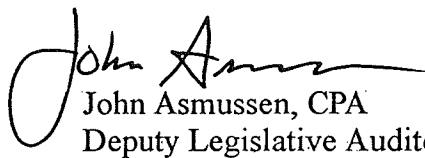
We also noted other matters involving the internal control structure and its operation that we reported to the management of the Office of the Attorney General at an exit conference held on April 23, 1993.

The results of our tests indicate that, except for the issues discussed in finding #1, with respect to the items tested, the Office of the Attorney General complied, in all material respects, with the provisions referred to in the audit scope paragraphs. With respect to items not tested, nothing came to our attention that caused us to believe that the Office of the Attorney General had not complied, in all material respects, with those provisions.

This report is intended for the information of the Legislative Audit Commission and management of the Office of the Attorney General. This restriction is not intended to limit the distribution of this report, which was released as a public document on August 20, 1993.

We thank the Office of the Attorney General staff for their cooperation during this audit.

  
James R. Nobles  
Legislative Auditor

  
John Asmussen, CPA  
Deputy Legislative Auditor

End of Fieldwork: March 19, 1993

Report Signed On: August 16, 1993





# Office of the Attorney General

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### Audit Participation

The following staff from the Office of the Legislative Auditor participated in this audit:

John Asmussen, CPA	Deputy Legislative Auditor
Claudia Gudvangen, CPA	Audit Manager
Dave Polisen, CPA	Auditor-In-Charge
Mary Annala, CPA	Staff Auditor
Carl Otto, CPA	Staff Auditor

### Exit Conference

An exit conference was held with the following staff from the Office of the Attorney General on April 23, 1993:

John R. Tunheim	Chief Deputy Attorney General
Joseph Reid	Administrative Manager



# Office of the Attorney General

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## Introduction

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The Office of the Attorney General was established by Article V of the Constitution of the State of Minnesota. Hubert H. Humphrey III is currently serving his third term as Attorney General. The Attorney General's main duties include providing legal advice, representing state agencies and their officials, and offering direct assistance to citizens of Minnesota. The Attorney General also represents Minnesota in civil and criminal cases and is a member of the Executive Council, the Pardons Board, the Land Exchange Board, and the State Board of Investment.

The Office of the Attorney General finances its activities primarily from general fund appropriations, which totalled \$19,963,000 for fiscal year 1992. The majority of office expenditures are for personnel costs. The following summary shows revenues and expenditures of the office for the year ended June 30, 1992:

Revenue:	
Billings for services	\$ 5,478,239
Litigation settlements	900,329
Other revenues	<u>1,516,350</u>
Total Revenue	<u>\$ 7,894,918</u>
Expenditures:	
Payroll	\$18,380,894
Other expenditures	<u>4,135,066</u>
Total Expenditures	<u>\$22,524,960</u>

Note: Expenditures do not include \$570,088 in payroll costs charged directly to other state agencies.

Source: Estimated/Actual Receipts and Manager's Financial Reports for Fiscal Year 1992 as of September 5, 1992.

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## Current Findings and Recommendations

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**1. The Attorney General's Office (AGO) has supplemented its appropriation authority by charging some attorneys' salaries directly to other state agencies.**

The AGO does not consistently assess agencies for the cost of services provided. We question whether the AGO has specific authority to charge attorneys' salaries directly to other state agencies. In addition, AGO billings have resulted in inequitable treatment for some agencies.

The AGO follows two different procedures to recover the cost of services provided to state agencies. Both are based, at least in part, on statutory requirements. However, the second practice has been expanded in recent years as the office's General Fund appropriation has been reduced through budget cuts.

Minn. Stat. Section 8.15 generally discusses recovery of Attorney General costs. It provides:

The attorney general in consultation with the commissioner of finance shall assess executive branch agencies a fee for legal services rendered to them. The assessment against appropriations from other than the general fund must be the full cost of providing the services. The assessment against appropriations supported by fees must be included in the fee calculation. The assessment against appropriations from the general fund not supported by fees must be one-half of the cost of providing the services.

The AGO deposits amounts collected from these billings as nondedicated receipts to the General Fund.

In 1991, the Legislature amended Minn. Stat. Section 8.06, which provides that the Attorney General shall act as the attorney for all state officers, boards or commissions in matters pertaining to their official duties. It also discusses the process for employing special attorneys. A sentence was added in 1991, as follows:

A state agency that is current with its billings from the attorney general for legal services may contract with the attorney general for additional legal and investigative services.

The AGO has used this provision as authority to initiate a different practice for recovery of costs. The office entered into interagency agreements with some state agencies. The office further interprets the statute to permit charging the salary and fringe benefits for certain attorneys directly to the other agencies appropriation accounts. The attorneys, however, remain

## Office of the Attorney General

under the supervision of AGO. For fiscal year 1992, payroll costs charged to other agencies totalled \$570,088. During the first six months of fiscal year 1993, the charges totalled \$768,208. The AGO has expanded use of interagency agreements because it has been unable to provide the same level of service from its appropriations.

We question whether the AGO has explicit statutory authority to have state agencies directly pay for the salaries of its attorneys. The AGO was able to offset its appropriation reductions by allowing state agencies to directly pay attorneys' salaries, rather than paying the cost itself and billing the agencies for reimbursement. For certain agencies, the services provided by the AGO under this arrangement were previously provided through the billing process. In addition, the AGO has interagency agreements with licensing boards and other agencies supported by fees which traditionally are not billed for services. Rather, the AGO notifies these agencies of the assessed amount, which they are to include in total costs when setting their fees or rates.

We have various other concerns about the AGO's billing process and the interagency agreements:

- There is no established process to ensure that state agencies which enter into interagency agreements pay only for services provided. Some state agencies pay for legal services provided to other agencies. The interagency agreements stipulate the amount of compensation and services the attorney will perform. The AGO sets up the estimated amount of time and the agency's allotment account to be charged on the payroll system. The agency pays the amount set up on the system regardless of the actual level of services provided. In some cases, the AGO may assign an attorney full time to an agency and the agency will pay 100 percent of the payroll costs. However, due to workload scheduling, that attorney may perform some services for another state agency. The original agency will continue to pay the attorney's salary unless they request an adjustment. The agency actually receiving the services will not be billed.
- Those state agencies with interagency agreements pay a lower rate than those which are assessed under the regular billing process. For fiscal year 1993, the regular billing rate for attorneys is \$51 per hour. The rate includes direct salaries, fringe benefits and support costs. Agencies who are under the interagency agreements pay only for direct salaries and fringe benefits; support costs are not included. For fiscal year 1993, the support cost component of the billing rate approximates \$17 per hour. Also, attorneys routinely work more than 80 hours per pay period, but only get paid for 80. Agencies under the agreements only pay the amounts set up on the payroll system which has a limit of 80 hours per pay period. The AGO assesses and bills other agencies for actual hours worked, which can exceed 80 hours per pay period.

## Office of the Attorney General

- The AGO is overcharging some agencies for services provided and undercharging others. Minn. Stat. Sect. 8.15 sets the assessment rates at 100 percent for nongeneral fund services and 50 percent for General Fund services provided. The AGO relies on the agency to identify the assessed rates based on the funding source for the program benefitted. However, the interagency agreements do not specify assessed rates and the agencies pay 100 percent of the attorneys' salary costs regardless of the funding source. Therefore, under these agreements, agencies which receive services for programs funded from the General Fund pay more than they would if they were a part of the regular billing process, even though support costs are not included. We identified seven attorneys whose full salaries were charged to various agencies' General Fund appropriations. In another instance, we found that, under the regular billing process, one department was assessed for all activities at the 50 percent rate, even though some of its programs had different funding sources.

Use of these interagency agreements appears to conflict with the statutes and appropriation laws governing AGO operations. Minn. Stat. Section 8.06 allows agencies to contract for additional legal services. However, neither the statute nor the AGO has defined what the basic level of services are and what constitutes special additional circumstances.

The 1993 Legislature instructed the Attorney General to establish a task force to review and make recommendations to the Legislature regarding funding options to pay for all legal services provided to executive branch agencies. Laws of 1993, Chapter 192, Section 11, Subd. 7, provides:

In order to increase the accountability of all parties and to simplify the current practices for paying for legal services, the attorney general shall establish a task force to review and make recommendations to the legislature regarding funding options to pay for all legal services provided to executive branch agencies. In addition to attorney general staff, members of the task force shall include fiscal staff from both houses of the legislature, staff of the department of finance, and staff from small and large executive branch client agencies. The ability to pay shall not be the only criteria used to allocate legal services. The task force shall study funding options that insure the availability of legal services from the attorney general's office essential to meet program needs of all executive branch agencies. The attorney general shall report the recommendations of the task force to the legislature by March 1, 1994.

### *Recommendations*

- *Upon completion of the task force report, the AGO should seek legislative clarification of the appropriate process for recovering the cost of services provided to state agencies.*

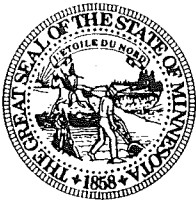
## Office of the Attorney General

### *Recommendations (Continued)*

- *If the AGO continues the use of interagency agreements, controls should be improved to ensure that:*
  - *agencies only pay for the actual services provided to them;*
  - *attorney costs are consistently charged at the proper funding source rate; and*
  - *agencies pay for the full cost of services provided, including support costs.*







# STATE OF MINNESOTA

## OFFICE OF THE ATTORNEY GENERAL

**HUBERT H. HUMPHREY III**  
ATTORNEY GENERAL

102 STATE CAPITOL  
ST. PAUL, MN 55155-1002  
TELEPHONE: (612) 296-6196

August 12, 1993

James R. Nobles  
Legislative Auditor  
Office of the Legislative Auditor  
Centennial Building  
St. Paul, MN 55155

Dear Mr. Nobles:

The Attorney General's Office(AGO) accepts your invitation and is pleased to have the opportunity to respond to the recommendations of the financial audit recently completed by members of your staff.

Although your report takes issue with the financing used by the AGO to provide legal services to some state agency clients, you found no material weakness in the financial operations of the AGO. There was no loss of taxpayer dollars. Furthermore, the report does not dispute that the money paid to the AGO by the agencies was for legal services provided to the agencies.

However, there is disagreement between Legislative Audit staff and the AGO over the intent of M. S. 8.06. When may a state agency contract with the AGO for legal services? Is it only when new legal services are sought by the agency or is it also when the AGO can not continue to provide a prior level of legal services needed by the agency? Is it necessary to define a pre-established base level of services, before the provisions of M. S. 8.06 can be used by the AGO and the agency?

The AGO disagrees with your conclusions regarding M. S. 8.06, but your report does address an area that is a concern to us as well. The current system for funding state legal services is confusing and fails to meet the total legal needs of state government. For this reason, the AGO prepared a proposal, which it submitted to the legislature during the 1993 session, to establish a task force to review the system and make recommendations to the legislature by March 1, 1994. The principal objective of the task force will be to determine how to build into the funding of legal services greater accountability across the board, at the legislature, in the executive branch agencies and in the AGO. We are in the process of establishing the task force and have invited you or a designee to participate in its work.

## **Reimbursement to General Fund**

Fifteen years ago the legislature and the AGO made a decision to consolidate the expenses of the AGO in the budget of the AGO. Before 1977, many of the payroll and other costs were budgeted by the agencies represented by the AGO. When the consolidation began in 1977, the legislature also had to make a procedural decision regarding how to budget for work done for programs funded with nongeneral fund dollars. Some of the choices available were to appropriate nongeneral fund dollars to the AGO for nongeneral fund work, or to appropriate general fund dollars to the AGO and then make an annual or biennial fund transfer to reimburse the general fund for any nongeneral fund expenditures, or to do a double appropriation, i.e., appropriate to the AGO from the general fund and appropriate to agencies from general and nongeneral funds as appropriate and then reimburse the general fund for services provided to nongeneral fund programs. The legislature at the recommendation of the AGO selected the latter of these three, the reimbursement option.

The reimbursement option was intended to be a simple process for transferring money from state dedicated funds to the state general fund. However, from the beginning there has been a considerable level of confusion. Most people familiar with the process assumed that the AGO received the money that agencies paid for their legal services. They did not understand that these payments in fact were not paid to the AGO, but instead were deposited directly in the general fund. The AGO was funded not by billings from agencies but by dollars appropriated by the legislature.

The level of confusion grew in 1985 when the legislature amended the purpose for billing agencies. Beginning with fiscal year 1986, most executive branch agencies were to be billed for a portion of the costs of providing legal services to them. A new purpose, increased accountability for legal expenditures, was added to the original purpose of reimbursing the general fund. The immediate effect of this amendment was to cut the general fund expenditures of the agencies impacted by the amendment. Also, because the general fund reimbursement rate was less than 100 percent, supporters of programs subject to the 100 percent rate, [for example, the hunting and fishing lobby,] argued that dedicated funds were not treated fairly. There was also now a double appropriation from the same fund. Money was appropriated from the general fund to the AGO and the agency for the same purpose.

In retrospect it would have been preferable for the legislature to appropriate from the general fund for general fund work and from the dedicated funds for dedicated fund work. No double appropriation would have resulted and there would

have been no need to create a special reimbursement system. As mentioned above, the purpose and practice of the AGO billings have been misunderstood from the start.

### **Interagency Agreements**

Apart from the reimbursement system, the AGO has for several years depended on interagency agreements with its state agency clients to finance and provide services that otherwise would not be provided. The agreements were not intended to be an independent form of reimbursement. They fit a different situation. Where they are used there is no double appropriation. Under the interagency agreement, the client agrees to pay the total cost of a full or part-time employee who would not be available to the client without the agreement. Thus, the cost to the client is the salary and fringe benefits paid to the employee assigned to the client. Because an AGO attorney paid under an interagency agreement may occasionally be called upon to assist another client, the original client could pay for assistance given to another client. We will build in safeguards to our process for monitoring attorney time to ensure that state agencies pay only for services they have agreed to pay for under the agreements.

The AGO sought and obtained authority for the interagency agreements in 1989, when the legislature passed Chapter 335, Art. 1, Sec. 12, subd. 8, with the following rider:

#### **Subd. 8. Base Cut**

\$(172,000)

\$(172,000)

Notwithstanding Minnesota Statutes, section 8.06 or other law, a state agency that is current with its billing from the attorney general for legal services may contract with the attorney general for additional legal and investigative services.

In 1991 Minnesota Statutes Chapter 8.06 was amended to include the rider language.

Since 1989, budget cuts have limited the ability of the AGO to meet the legal needs of some of its clients. In addition, legislative committees have made decisions which avoided the double appropriation and appropriated money to agencies to contract with the AGO for legal services. As a result, the number of interagency agreements has grown. The growth of this practice was described in budget documents in 1991 and again in 1993.

One [budget] alternative is to continue existing interagency agreements and enter new ones with state agency clients who would directly fund the unfunded or new positions needed to represent that agency.

Page 107, 1992-93 Biennial Budget.

The Attorney General has had to appoint outside counsel, delegate authority to agencies to perform certain legal services, and contract with clients for services that could not be provided otherwise. This patchwork of funding, delegations and agreements limits the flexibility of the Attorney General to direct staff and resources to top priorities. However, it maintains the Attorney General's authority and duty to represent the state as a whole and to assure fundamental fairness and consistent application of all relevant laws in the public interest(M.S. 8.01 and 8.06).

Page E-395, 1994-5 Biennial Budget.

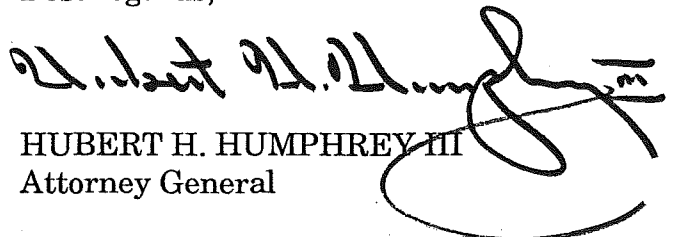
## **Recommendations**

The task force was proposed to give the AGO, the legislature and our state agency clients an opportunity to take an indepth look at how state legal services are financed and to propose funding mechanisms that can reconcile the need to increase the accountability of all parties and to ensure adequate representation of the state's legal interests. A central purpose of the proposal was to seek the type of clarification you have recommended.

Controls regarding the processing of interagency agreements are being improved. Reports on attorney time will be monitored to ensure that state agencies pay for only the services contracted for under the agreements.

It has been a pleasure to work with you and your audit staff. If I or my staff can be of any further assistance, please contact me.

Best regards,

  
HUBERT H. HUMPHREY III  
Attorney General