
Office of the State Auditor

**Financial Related Audit
For the Two Years Ended December 31, 1998**

July 1999

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**Financial Audit Division
Office of the Legislative Auditor
State of Minnesota**

99-40

SUMMARY

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Office of the State Auditor

Financial Related Audit For the Two Years Ended December 31, 1998

Public Release Date: July 29, 1999

No. 99-40

Agency Background

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, the current State Auditor, began her second term in January 1999. The State Auditor serves on the State's Executive Council, State Board of Investment, Land Exchange Board, Minnesota State Housing Finance Agency Board, Rural Finance Authority Board, Public Employees Retirement Association Board, and the Board of Government Innovation and Cooperation.

The OSA receives support for its operations in the form of state appropriations. Minn. Stat. Section 6.58 requires the OSA to bill audit clients for the costs of audits and examinations at a rate sufficient to cover the cost of its audits. The audit practice receipts collected from clients are deposited as nondedicated receipts in a special revenue fund account.

Audit Scope and Conclusions

Our audit scope included a review of the Office of the State Auditor's appropriation, audit practice revenue, personnel services, and other administrative expenditures for the period from January 1, 1997, through December 31, 1998.

We concluded that the OSA appropriately managed its financial operations and ensured that its revenues and expenditures were accurately accounted for. The OSA spent its state appropriation within its appropriation authority.

We also audited the OSA's audit practice revenue obtained through reimbursements of OSA client audit costs. We concluded that the OSA properly billed for audit costs and properly processed and collected audit practice receipts. The State Auditor generated sufficient revenues to recover reimbursable audit costs.

In addition, we audited OSA expenditures including personnel services and other administrative expenditures. The OSA properly processed and recorded payroll transactions, and the transactions we tested complied with applicable legal requirements.

Other administrative expenditures we reviewed included rent, travel, and supplies and equipment. We verified the reliability of accounting procedures and accurate processing of these transactions. For the transactions tested, the OSA properly and accurately processed and recorded the expenditures.



STATE OF MINNESOTA
OFFICE OF THE LEGISLATIVE AUDITOR
JAMES R. NOBLES, LEGISLATIVE AUDITOR

Representative Dan McElroy, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

The Honorable Judith Dutcher
State Auditor

We have audited the Office of the State Auditor for the period January 1, 1997, through December 31, 1998, as further explained in Chapter 1. Our audit scope included audit practice receipts, payroll, and other administrative expenditures including rent, travel, and supplies and equipment, as well as appropriation control.

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 Office of the State Auditor complied with provisions of laws, regulations, and contracts 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 for compliance 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 the State Auditor. This restriction is not intended to limit the distribution of this report, which was released as a public document on July 29, 1999.

James R. Nobles
Legislative Auditor

Claudia J. Gudvangen, CPA
Deputy Legislative Auditor

End of Fieldwork: June 14, 1999

Report Signed On: July 22, 1999

Office of the State Auditor

Table of Contents

	Page
Chapter 1. Introduction	1
Chapter 2. Appropriation Control	3
Chapter 3. Audit Practice Revenue	5
Chapter 4. Payroll and Other Administrative Expenditures	7
Status of Prior Audit Issues	10

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
Carl Otto, CPA	Auditor-in-Charge
Charlie Klein	Auditor

Exit Conference

This report was discussed with the following staff of the Office of the State Auditor on July 20, 1999:

Jennifer Mohlenhoff	Assistant State Auditor
Greg Hierlinger	Deputy State Auditor, Audit Practice
Virginia Davis	Director of Finance

Chapter 1. Introduction

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 is the current State Auditor. She began her second term in January 1999. The State Auditor serves on the State's Executive Council, State Board of Investment, Land Exchange Board, Minnesota State Housing Finance Agency Board, Rural Finance Authority Board, Public Employees Retirement Association Board, and the Board of Government Innovation and Cooperation.

The OSA is divided into seven divisions:

- The Constitutional Office Division oversees the operation of the Office of the State Auditor.
- The Audit Practices Division conducts annual financial audits of organizations affiliated with counties and cities, police and fire relief associations, and other local governments throughout the state.
- The Government Information Division promotes financial accountability and cost effective public services in local government.
- The Special Investigations Division promotes integrity and accountability in local government by investigating allegations of wrongdoing uncovered or suspected.
- The Pension Oversight Division monitors investment, financial, and actuarial reporting for public pension funds to ensure financially stable retirement systems and compliance with Minnesota statutes governing the activities of relief associations.
- The Single Audit Division determines if single audit reports submitted to the OSA comply with reporting requirements of the Single Audit Act of 1984, as amended in 1996, the Office of Management and Budget Circular A-133.
- The Tax Increment Financing Division audits and monitors the financial condition and legal compliance of tax increment financing districts throughout the state.

OSA activities, except for those of the Tax Increment Financing Division, are financed through General Fund appropriations. The OSA's appropriations for fiscal years 1997, 1998, and 1999 were \$7,144,000, \$7,718,000, and \$7,916,000, respectively. A 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. We discuss appropriations and local government offsets more fully in Chapter 2.

Minn. Stat. Section 6.58 requires that the State Auditor collect fees from audited organizations to cover the cost of its audits. The Audit Practices Division bills the political subdivisions it audits

Office of the State Auditor

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 to a special revenue account. 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 State Auditor for fiscal year 1998.

Table 1-1	
Summary of OSA Financial Activity	
Fiscal Year 1998	
	Fiscal Year <u>1998</u>
Sources:	
General Fund:	
Operating Appropriation	\$7,718,000
Less Appropriation Reduction	(8,519)
Transfer In – TIF Account (2)	282,942
Balance Forward In – TIF Account (2)	25,000
Special Revenue Fund:	
Dedicated Revenue (1)	15,943
Balance Forward In	6,078
Total Sources	<u>\$8,039,444</u>
Uses:	
Expenditures:	
Payroll	\$6,212,187
Rent	272,532
Travel, In and Out State	173,438
Supplies	19,048
Capital Equipment	59,427
Miscellaneous Expenditures	199,206
Total Expenditures	<u>\$7,035,838</u>
Other Uses:	
Balance Forward Out – General Fund	994,093
Balance Forward Out – Special Revenue Fund	8,162
Transfer Out - TIF Fund (2)	1,351
Total Other Uses	<u>\$1,003,606</u>
Total Uses	<u>\$8,039,444</u>

Notes:

- (1) Dedicated revenue is collected for seminar and workshop activities.
- (2) Minn. Stat. Section 469.177, Subd. 11 created the TIF division. The division received funding from a .10 percent charge on TIF districts in fiscal year 1998. The charge increased to .25 percent in fiscal year 1999. The State Treasurer collects the funds, deposits the money in the General Fund, and then transfers the funds to the State Auditor. Prior to fiscal year 1998, the State Auditor recorded the TIF money in a Special Revenue Fund. They now record the money in the General Fund.

Source: Minnesota Accounting and Procurement System, Allotment Balance within Appropriation Report as of September 1998.

Chapter 2. Appropriation Control

Chapter Conclusions

The Office of the State Auditor complied with appropriation laws and operated within its legally authorized funding level. Expenditures were charged to the proper fiscal year on the state's accounting system. Residual funds were canceled or carried forward as required by law.

Background

The State Auditor received funding for its operations through a General Fund appropriation. The State Auditor allocates the appropriation to five operating divisions and accounts for expenditures by division. Table 2-1 summarizes financial activity for these divisions for fiscal year 1998.

Table 2-1
Summary of General Fund Appropriation
Allocation for Fiscal Year 1998

<u>Division</u>	<u>Appropriation</u>	<u>Amount Expended</u>	<u>Balance Forward to FY 1999</u>
Audit Practice (includes Single Audit)	\$5,975,437	\$5,407,331	\$568,106
Government Information	603,585	428,123	175,462
Special Investigations	431,673	354,372	77,301
Constitutional Office	309,000	294,682	14,318
Pension Oversight	<u>389,786</u>	<u>305,218</u>	<u>84,568</u>
Total Appropriation	<u>\$7,709,481</u>	<u>\$6,789,726</u>	<u>\$919,755</u>

Source: Minnesota Accounting and Procurement System, Allotment Balance within Appropriation Report as of September 1998.

A 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. In accordance with Minn. Stat. Section 477A.014, Subd. 4, the State Auditor certifies costs related to the government information function to the Department of Revenue for a reduction in local government aids. The local government aid offset is limited to \$217,000 per year. The State Auditor also certifies costs related to the Pension Oversight 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

Office of the State Auditor

aids by the amount of State Auditor costs associated with the audits or exams of the police and firefighters relief associations.

In addition to the General Fund appropriation, the State Auditor receives funding for the cost of examining the use of tax increment financing. Under Minn. Stat. Section 469.177, Subd. 11, the TIF division received funding from a .10 percent charge on tax increment financing districts in fiscal year 1998. The rate increased to .25 percent in fiscal year 1999. The State Treasurer collects the funds from the county treasurers, deposits the money in the General Fund, and subsequently transfers the funds to the State Auditor. Revenue collections in fiscal year 1998 totaled \$281,592 for examinations of tax increment financing districts. Total expenditures in fiscal year 1998 were \$233,606.

Audit Objectives and Methodology

Our audit of OSA appropriations addressed the following questions:

- Did the office comply with appropriation laws?
- Were expenditures charged to the appropriate fiscal year?
- 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 Office of the State Auditor complied with the provisions of the appropriation laws and operated within its legally authorized funding level. Expenditures were charged to the proper fiscal year. Residual funds were administered in the proper manner required by law.

Chapter 3. Audit Practice Revenue

Chapter Conclusions

The Office of the State Auditor properly processed and collected audit practice receipts. The State Auditor generated sufficient revenues to recover reimbursable audit costs.

Background

The State Auditor is responsible for collecting fees from audited organizations to recover audit costs. Minn. Stat. Section 6.58 states that the General Fund shall be used to provide personnel, pay other expenses, and to acquire equipment used in connection with reimbursable examinations and other duties pursuant to law. The law also states that the State Auditor shall review and adjust the schedule of charges for such examinations at least annually to insure that the amount collected is sufficient to pay all costs connected with such examinations during the fiscal year. The State Auditor, by authority of Minn. Stat. Section 16A. 6701, deposits audit practice receipts into a special revenue account. These receipts, however, are not available for expenditure by the State Auditor.

For fiscal year 1998, the State Auditor collected approximately \$5,750,000 in audit practice receipts. Audit clients with current work-in-progress are billed on a monthly basis. Approved audit charges and auditor expenses are the basis for billing a client. The State Auditor has the authority to charge interest on delinquent accounts of undisputed bills that are 60 days past due.

Audit Objectives and Methodology

The primary objectives of our audit of audit practice revenues were to answer the following questions:

- Did the Office of the State Auditor properly collect and deposit audit practice receipts?
- Were billings accurate and sufficient to recover audit practice costs?

To meet these objectives, we interviewed office employees to gain an understanding of the internal control structure over the billing and collection process. We analyzed audit practice revenue transactions to determine proper recording of receipts, reviewed source documents to determine proper authorization, and tested client payments to ensure proper collection and deposit pursuant to Minnesota Statutes.

Office of the State Auditor

Conclusions

The Office of the State Auditor properly processed, collected, and deposited audit practice receipts. The office generated sufficient revenues to recover reimbursable audit costs. The State Auditor, as required by Minn. Stat. Section 6.58, completed an annual overall evaluation of revenues and expenditures to determine the accuracy of its billing rates.

Chapter 4. Payroll and Other Administrative Expenditures

Chapter Conclusions

The Office of the State Auditor appropriately processed and recorded payroll and other administrative expenditure transactions. The expenditures were allocated to the appropriate divisions. The office complied with applicable finance-related legal provisions and bargaining unit agreements for the items tested.

Background

The Office of the State Auditor incurs administrative expenditures for personnel services, travel, supplies and equipment, rent, and other miscellaneous expenses. Personnel services represented over 88 percent of total expenditures. Travel, rent, and supplies and equipment represent the majority of other administrative expenditures. We discuss payroll and other administrative expenditures in the following sections.

Payroll

The Office of the State Auditor employs approximately 130 employees located in offices throughout the state. The employees are covered by various bargaining unit agreements. The OSA also 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 1998.

**Table 4-1
Payroll Expenditures
Budget Fiscal Year 1998**

<u>Payroll Type</u>	<u>Amount</u>
Full-time Salaries	\$6,011,297
Part-time Salaries	46,967
Overtime	106,249
Severance/Vacation Payoffs/Other	<u>47,674</u>
Total Payroll	<u>\$6,212,187</u>

Sources: OLA summary of expenditures for budget fiscal year 1998 through December 31, 1998.

Office of the State Auditor

Bi-weekly payroll transactions and pay rate changes are processed through the Department of Employee Relations' State Employee Management System (SEMA4). These transactions are also recorded in the Minnesota Accounting and Procurement System (MAPS) through a computer system interface.

Audit Objectives and Methodology

While conducting our audit, we considered the following objectives:

- Were employees paid in accordance with material finance-related provisions of state bargaining unit agreements?
- Were payroll transactions accurately recorded in the state's accounting systems and allocated to the appropriate divisions?

The methodology we used to audit these objectives included inquiries 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, reasonableness, and proper recording in the accounting system.

Conclusions

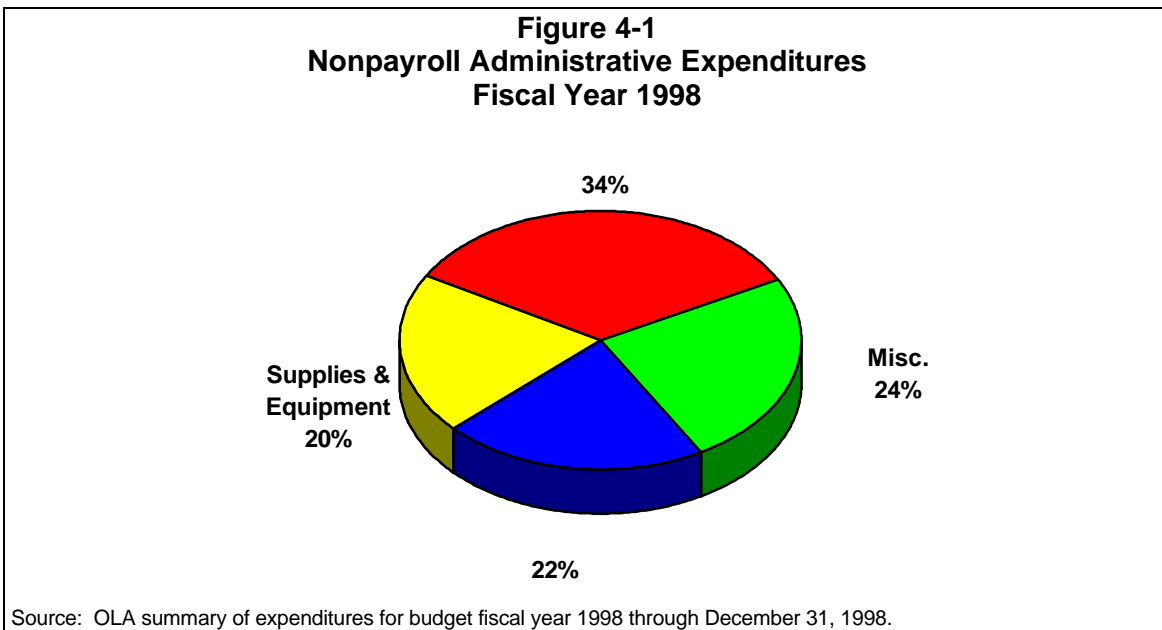
Based on our testing, the State Auditor complied with material finance related provisions of state bargaining unit agreements. In addition, the State Auditor's payroll transactions were accurately recorded in the state's accounting systems and allocated to the appropriate divisions.

Other (Nonpayroll) Administrative Expenditures

Other administrative expenditures accounted for approximately 12 percent of total operating costs. The State Auditor incurred administrative expenditures in the following categories: rent, travel, supplies and equipment, and other miscellaneous expenses.

The largest nonpayroll 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 State Auditor is currently leasing office space for employees in eight separate cities. For fiscal year 1998, the office paid approximately \$272,000 for rent. This amount includes payments for office space, equipment rentals, room rentals, and parking spaces.

Figure 4-1 illustrates the fiscal year 1998 nonpayroll administrative expenditures by type. The miscellaneous category on the chart is comprised mainly of professional/technical services, purchased services, and communication expenses.



Audit Objectives and Methodology

We focused our review of rent, travel, and supplies and equipment expenditures on the following objectives:

- Were expenditures properly recorded in the state’s accounting system?
- Did expenditures comply with state accounting policies and procedures?
- Were expenditures charged to the appropriate division?

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

Conclusions

The State Auditor properly and accurately recorded expenditures in the accounting system and allocated expenditures to the appropriate division. For the items tested, the State Auditor complied with applicable accounting policies and procedures.

**Status of Prior Audit Issues
As of June 14, 1999**

May 16, 1997, Legislative Audit Report 97-30 covered the two years ended December 31, 1996. 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. The audit was conducted in accordance with the Legislative Audit Commission policy to perform financial audits of constitutional officers at both mid-term and end of the term.

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.