OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

Financial Audit Division Report

Bureau of Mediation Services

Fiscal Years 2002 through 2004

FEBRUARY 24, 2005 **05-12**

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).

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

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OLA

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

Mr. James Cunningham, Commissioner
Bureau of Mediation Services

We have audited the financial activities of the Bureau of Mediation Services (Bureau) for the period July 1, 2001, through June 30, 2004. Our audit scope included employee payroll, grants, rent, employee travel reimbursements, and professional/technical services. The Report Summary highlights our overall audit conclusions. The specific audit objectives and conclusions are contained in the individual chapters of this report.

We selected the Bureau of Mediation Services for audit based on our annual assessment of state agencies and programs. We used various criteria to determine the entities to audit, including the size and type of each agency's financial operations, length of time since the last audit, changes in organizational structure and key personnel, and available audit resources.

We conducted our audit in accordance with *Government Auditing Standards,* issued by the Comptroller General of the United States. Those standards require that we obtain an understanding of the center's internal controls relevant to the audit objectives. We used the guidance contained in *Internal Control-Integrated Framework*, published by the Committee of Sponsoring Organizations of the Treadway Commission, as our criteria to evaluate agency controls.

The standards also require that we plan the audit to provide reasonable assurance that the Bureau of Mediation Services complied with financial-related legal provisions that are significant to the audit. In determining the Bureau's compliance with legal provisions, we considered requirements of laws, regulations, contracts, and grant agreements.

To meet the audit objectives, we gained an understanding of the Bureau of Mediation Services' financial policies and procedures. We considered the risk of misstatements in the accounting records and noncompliance with relevant legal provisions. We analyzed accounting data to identify unusual trends or significant changes in financial operations. We examined a sample of evidence supporting the Bureau's internal controls and compliance with laws, regulations, contracts, and grant provisions.

/s/ James R. Nobles

James R. Nobles
Legislative Auditor

/s/ Claudia J. Gudvangen

Claudia J. Gudvangen, CPA
Deputy Legislative Auditor

End of Fieldwork: January 3, 2005

Report Signed On: February 18, 2005

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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
David Poliseno, CPA, CISA	Audit Manager
Susan Mady	Auditor-in-Charge

Exit Conference

We discussed the results of the audit with the following staff of the Bureau of Mediation Services at an exit conference on February 15, 2005:

James Cunningham	Commissioner
Steve Hoffmeyer	Deputy Commissioner
Deanna Matteson	Accounting Officer

Report Summary

Conclusion:

The Bureau of Mediation Services' internal controls provided reasonable assurance that its operating expenditures were accurately reported in the accounting records and in compliance with applicable legal provisions and management's authorization. However, we identified a concern with the Bureau's administration of its Labor-Management Cooperative grants.

Finding:

- The Bureau did not administer its Labor-Management Cooperative grants in compliance with applicable rules and grant agreement requirements. (Finding 1, page 10)

The audit report contained one audit finding relating to legal compliance. The prior audit report did not contain any audit findings.

Audit Scope:

Audit Period:
Fiscal Years 2002 through 2004

Selected Audit Areas:
- Payroll
- Rent
- Travel Reimbursements
- Professional/Technical Services
- Grant Expenditures

Background:

The Bureau of Mediation Services attempts to keep labor disputes at a minimum by ensuring that constructive labor-management relationships exist in the state's public, nonprofit, and private sectors. The Bureau is financed primarily by a General Fund appropriation, which was $1,773,000 in fiscal year 2004.

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Chapter 1. Introduction

The Legislature enacted the Minnesota Labor Relations Act in 1939 as a means to peacefully settle labor disputes. To administer the Act, the Legislature created the Division of Conciliation. In 1969, the Division of Conciliation was established as a separate state agency and renamed the Bureau of Mediation Services. It operates pursuant to Minn. Stat. Section 179.02. It attempts to keep labor disputes at a minimum by ensuring that constructive labor-management relationships exist in the state's public, nonprofit, and private sectors. In 1993, the Legislature transferred the responsibilities of the Office of Dispute Resolution from the Department of Administration to the Bureau. James Cunningham was appointed the Bureau's commissioner on February 10, 2003, replacing Lance Teachworth, who retired.

The Bureau of Mediation Services employs 15 staff in four divisions:

- The **Mediation Unit** assists labor and management in resolving collective bargaining unit disputes, including labor contracts and grievances.
- The **Labor-Management Cooperation Unit** awards matching grant funds to labor-management committees and councils for support of public and private sector labor organizations.
- The **Representation Unit** resolves issues resulting from new bargaining unit structures and employee groups desiring representation by a labor union. It also resolves fair share fee challenges and assists with union elections, if requested.
- The **Alternative Dispute Resolution Unit** provides third-party mediation or facilitation to resolve public agency nonlabor disputes without resorting to litigation.

The Bureau receives the majority of its funding from state appropriations. The agency also receives dedicated revenues from interagency agreements and seminar and workshop fees. Table 1-1 shows the financial activity of the Bureau for the audit period.

Table 1-1
Bureau of Mediation Services
Sources and Uses of Funds

	Fiscal Year 2002	Fiscal Year 2003	Fiscal Year 2004
Sources:			
State Appropriations	$2,259,000	$2,307,000	$1,773,000
Interagency Receipts	100,652	39,626	0
Other Receipts	31,760	747	2,427
Transfer In	10,000	220,000	0
Balance Forward In	64,910	146,837	141,905
Total Sources	$2,466,322	$2,714,210	$1,917,332
Uses:			
Payroll	$1,631,535	$1,636,942	$1,433,086
Rent	149,116	142,464	142,990
Travel	89,272	80,865	75,504
Professional/Technical Services	72,129	136,363	71,239
Grants (Note 1)	263,500	0	97,000
Other Expenditures	83,933	128,472	44,243
Total Expenditures	$2,289,485	$2,125,106	$1,864,062
Balance Forward Out	146,837	141,905	39,770
Cancellations (Note 2)	30,000	385,503	13,500
Transfers Out	0	61,696	0
Total Uses	$2,466,322	$2,714,210	$1,917,332

Note 1: For fiscal year 2003, the Legislature cancelled the Bureau's Labor-Management Cooperative grants and any remaining funds for grants were returned to the General Fund. However, for fiscal year 2004, the Legislature reinstated funding for these grants.

Note 2: The amount cancelled in fiscal year 2003 includes a reduction of $347,000 (unallotment) per Minn. Stat. Section 16A.152, subd. 4.

Source: Minnesota Accounting and Procurement System (MAPS) for fiscal years 2002, 2003, and 2004 as of December 31, 2004.

Chapter 2. Operating Expenditures

Chapter Conclusions

The Bureau of Mediation Services' internal controls provided reasonable assurance that operating expenditures were accurately reported in the accounting records and in compliance with applicable legal provisions and management's authorization. The Bureau accurately compensated and reimbursed its employees in compliance with applicable bargaining agreements and compensation plans.

For the items tested, employees were paid and reimbursed for travel in accordance with the provisions of applicable plans and the Bureau policies. We determined that the Bureau accurately paid and recorded rent based on authorized lease agreements. We also found that the agency's internal controls provided reasonable assurance that payments for professional services were authorized, based on work performed, and accurately reported in the accounting records.

Audit Objective

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

- Did the Bureau's internal controls provide reasonable assurance that operating expenditures were accurately reported in the accounting records and in compliance with applicable finance-related legal provisions and management's authorization?

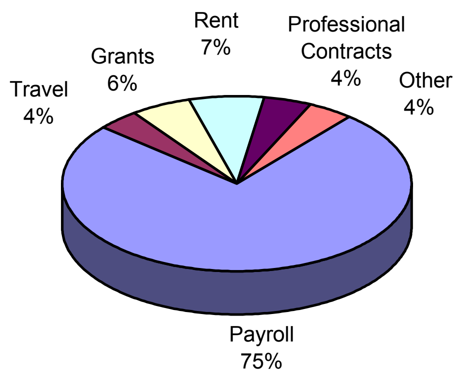
- Did the Bureau compensate and reimburse its employees in accordance with applicable bargaining agreements and compensation plans?

- For the items tested, did the Bureau comply with significant finance-related legal provision?

Background Information

Payroll represents the Bureau of Mediation Services' largest expenditure. In addition to payroll, the agency incurred other costs for rent, employee travel reimbursements, and purchased, professional, and technical services. The Bureau also provided grant funds to eligible organizations, as discussed in Chapter 3. Figure 2-1 shows the percentage of expenditures by type for the three fiscal years ended June 30, 2004.

Figure 2-1
Expenditures by Type
Three Fiscal Years Ended June 30, 2004



Source: Minnesota Accounting and Procurement System (MAPS) for fiscal years 2002, 2003, and 2004 as of December 31, 2004.

Payroll

During the audit period, the Bureau of Mediation Services spent approximately $1.6 million per year on salary and benefits for its 15 employees. The Bureau's accounting officer is responsible for processing the biweekly payroll in the state's payroll system (SEMA4), and the commissioner's assistant handles the human resources functions. Each of these individuals has backup responsibility for the other, creating incompatible access to both human resources and payroll functions. However, due to limited staff size, Bureau management has decided to accept this risk, as it cannot feasibly separate access. As an alternative control, the Bureau has instituted detective controls to review the work of staff with access to these incompatible functions. For example, the commissioner reviews and approves the biweekly SEMA4 payroll output reports.

Rent

During the audit period, the Bureau paid rent for two St. Paul offices: one for the Bureau's main office and the other for the Office of Dispute Resolution. The Bureau's current office space lease began on November 1, 1998, and is effective for ten years. In fiscal year 2003, at the end of its lease, the Bureau moved the Office of Dispute Resolution to the main office space.

Travel

The Bureau incurred about $80,000 each year for travel expenditures. The majority of staff use the Bureau's assigned state car to handle state business; however, individuals also use their own vehicles and are reimbursed for mileage. These individuals also incur meal, lodging, and other travel-related expenditures. The Bureau reimbursed staff for eligible travel expenses in amounts allowed in the Managerial and Commissioner's Plans and as specified further in the Bureau's travel policy.

Professional/Technical Services

The Bureau utilized professional and technical services in its operations. It incurred approximately $90,000 each year for services rendered by vendors and contractors. The Bureau has specific procedures for procurement, authorization, and payment for these services. As a control, the commissioner reviews invoices, contracts, and monthly expenditure reports, which detail all expenditures processed by the accounting officer.

There were no findings related to operating expenditures.

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Chapter 3. Labor-Management Cooperation Grants

Chapter Conclusions

The Bureau of Mediation Services' internal controls provided reasonable assurance that Labor-Management Cooperation grant expenditures were accurately reported in the accounting records and in compliance with management's authorization.

The Bureau did not comply with certain legal provisions applicable to the grants. We found inconsistencies between the applicable statutes, rules and grant agreements. Further, the Bureau did not enforce certain grant agreement requirements, such as the grantees undergoing compliance audits or submitting quarterly financial reports in a timely manner.

In fiscal year 2002, the Bureau of Mediation Services received an appropriation of $302,000 for Labor-Management Cooperation grants. The grants provide financial and technical assistance for eligible labor-management organizations to fund start up and ongoing operating costs. In fiscal year 2003, the Legislature cut all funding to this program. However, in fiscal year 2004, the Bureau received a $100,000 appropriation for these grants.

To request a grant, the labor-management organizations must submit an application identifying committee goals and planned use of the grant funds. In addition to the application, they must submit separate work and financial plans. Organizations can apply for an annual maximum grant of $75,000, as outlined in Minn. Stat. Section 179.85. The organizations can reapply each year for continued grant funding. The Bureau's commissioner and program director review grant applications, determine awards, and monitor the progress of the grants. As established in Minnesota Rules, the grant award is for a 12-month period, which begins in January of each year.

The committees and councils submit a quarterly request to receive payment of grant funds. Minn. Stat. Section 179.85 also requires the grant recipient to provide a nonstate match of 10 percent during the first year of the grant, 20 percent in the second year, and 50 percent in the third and subsequent years.

Currently, Minnesota has eight area/industry labor-management organizations. Table 3-1 shows the amount the Bureau disbursed during the audit period for its Labor-Management Cooperation grants.

Table 3-1
Bureau of Mediation Services
Labor-Management Grants
Fiscal Years 2002 – 2004

Grant Recipients	2002	2003	2004
Construction Industry Research Company	$ 18,000	$ 0	$ 2,000
Construction Partnership, Inc.	20,000	0	0
Iron Range Labor-Management Association	0	0	2,000
Labor-Users-Contractors Council	40,000	0	12,000
Lake Superior Area Labor-Management Association	63,000	0	34,000
Mississippi Valley Labor-Management Council	10,000	0	1,000
Twin City Area Labor-Management Council	68,000	0	40,000
Twin Ports Construction Liaison Council	4,500	0	2,000
Upper Midwest Labor Management Council	40,000	0	0
Labor Management Health Council	0	0	4,000
Total	$263,500	$ 0	$97,000

Source: Minnesota Accounting and Procurement System (MAPS) expenditures for fiscal years 2002, 2003, and 2004 as of December 31, 2004.

Audit Objectives

Our audit of the Labor-Management Cooperation grant expenditures focused on the following questions:

- Did the Bureau's internal controls provide reasonable assurance that grant expenditures were accurately reported in the accounting records and in compliance with management's authorization?
- Did the Bureau's Labor-Management Cooperative grant expenditures comply with significant finance-related legal provisions?

Audit Finding and Recommendations

1. The Bureau of Mediation Services did not administer its Labor-Management Cooperative grants in compliance with applicable program rules and grant agreement provisions.

The Bureau provided grants to eligible labor-management committees and councils to fund start up and ongoing operating costs. The labor-management councils are comprised of employers and labor unions whose goals are to improve labor-management in their specific geographic region or area of the state. The Bureau evaluated the need for new councils and assisted councils to organize and train board members and design needed programs and services. The Bureau also worked with councils to establish a long-range plan to help assure their continued viability.

Our review of the grants disclosed the following weaknesses:

- The rules and grant agreements contain conflicting language. The Bureau's statutes give them the authority to administer these grants, while the rules dictate the process that it will follow. The grant agreements stipulate each party's rights and responsibilities. We found several instances where certain provisions were not consistent between the rules and grant agreements. For example, Minnesota Rule 5520.0300 states that the grant period is on a calendar-year basis, but the grant agreement requires a fiscal year term. Also, Minnesota Rule 5520.0560 requires quarterly financial and activity reports to be submitted within 20 days after the quarter end, while the grant agreement did not specify any filing dates. As a result, the Bureau did not receive all of the reports in a timely manner.

- The grantees did not comply with all the provisions in Minnesota Rule 5520.0620 regarding audits. The rule requires all grant recipients to have a financial and compliance audit at least once every two years. It also lists specific audit objectives and identifies information and comments to be included in the audit report. Most grantees had an independent audit with an opinion on their financial statements. However, the audit reports did not address all of the internal control and compliance issues required by the rule. Audits help to ensure that grantees spend funds in accordance with applicable regulations. However, because these grants are often quite small, requiring expanded compliance audits may not be cost beneficial. The Bureau could implement less costly monitoring activities and still obtain the desired results.

The Bureau needs to review the grant program and the related legal compliance requirements and establish a cost effective control structure. The Bureau should then ensure that all of the legal provisions and the grant agreements are consistent.

Recommendations

- *The Bureau of Mediation Services should ensure that provisions contained in the rules and grant agreements are consistent and enforced.*

- *The Bureau should review the grant agreement provisions, such as the audit requirements, and evaluate the cost/benefit of each provision.*

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Status of Prior Audit Issues
As of January 3, 2005

Most Recent Audit

Legislative Audit Report 00-23, issued in May 2000, covered the three fiscal years ended June 30, 1999. The scope of this audit included payroll, administrative and grants expenditures, and interagency revenues. The report did not have any written findings.

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 and 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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BMS

BUREAU OF MEDIATION SERVICES

State of Minnesota

February 22, 2005

Mr. James R. Nobles
Legislative Auditor
Room 140 Centennial Building
658 Cedar Street
St. Paul, MN 55155

This letter is in response to the draft audit report for audit work completed regarding the Bureau of Mediation Services for the period July 1, 2001, through June 30, 2004.

I appreciated the opportunity to review the draft report with your staff on Tuesday, February 15, 2005, and hereby offer the following responses to Findings and Recommendations contained in the Report.

Audit Finding No. 1: "The Bureau of Mediation Services did not administer its Labor-Management Cooperative grants in compliance with applicable program rules and grant agreement provisions."

Audit Recommendation: "The Bureau of Mediation Services should ensure that provisions contained in the rules and grant agreements are consistent and enforced."

"The Bureau should review the grant agreement provisions, such as the audit requirements, and evaluate the cost/benefit of each provision."

BMS response: The Bureau has initiated the process to update the grant rules to conform with the grant agreements. This process has been initiated by myself and my assistant, Carol S. Clifford, and should be completed by September 2005.

The Bureau changed the effective date of the grant contracts from January to July in our 2004-2005 appropriation language. The change in the grant period was done to assist several grantee organizations so they could remain operational after losing funding due to the unallotment of 2003 grant funds and an overall grant reduction in the 2004-2005 biennial budget. Changing the grant period allowed the grantee organizations to receive funding at a diminished level six months sooner than they would have otherwise. Our agency rules were not changed at that time due to the uncertainty of continued funding for the grant program.

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The Bureau has also taken steps to monitor and ensure that the quarterly financial and activity reports are submitted by grantees on a timely basis. Future grant contracts will contain language reflecting report timelines. The grant rules pertaining to audit requirements will also be revised so that financial accountability is maintained in a more cost effective manner.

We wish to thank you and your staff for the professionalism with which the audit was conducted and the courtesies extended to us in the review process.

Sincerely,

/s/ James A. Cunningham, Jr.

James A. Cunningham, Jr.
Commissioner

JAC:dm

Enclosures