

State of Minnesota



Office of the State Auditor

Julie Blaha
State Auditor

City of Duluth
(Including the Duluth
Economic Development Authority)
Duluth, Minnesota

Management and Compliance Report

Year Ended December 31, 2023

City of Duluth Duluth, Minnesota

Table of Contents

	<u>Page</u>
City of Duluth Management and Compliance Report	
Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	1
Report on Compliance for Each Major Federal Program and Report on Internal Control Over Compliance Required by the Uniform Guidance	3
Schedule of Findings and Questioned Costs	6
Corrective Action Plan	9
Duluth Economic Development Authority Management and Compliance Report	
Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	11

**City of Duluth
Management and Compliance Report
Year Ended December 31, 2023**



**Report on Internal Control Over Financial Reporting and on Compliance and
Other Matters Based on an Audit of Financial Statements Performed in
Accordance with *Government Auditing Standards***

Independent Auditor's Report

The Honorable Roger Reinert, Mayor,
and Members of the City Council
City of Duluth, Minnesota

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Duluth, Minnesota, as of and for the year ended December 31, 2023, and the related notes to the financial statements, which collectively comprise the City's basic financial statements, and have issued our report thereon dated June 20, 2024. These financial statements include the activities of the Spirit Mountain Recreation Area Authority component unit for the year ended April 30, 2023. We issue separate management and compliance reports for the Duluth Airport Authority, the Duluth Entertainment and Convention Center Authority, the Duluth Transit Authority, and the Spirit Mountain Recreation Area Authority component units. This report does not include the results of our audit testing of these component units' internal control over financial reporting or on compliance and other matters. This report also does not include the results of our audit testing of the Duluth Economic Development Authority component unit's internal control over financial reporting or compliance and other matters that are reported on separately within the Management and Compliance Report.

Report on Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the City of Duluth's internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing our opinion on the effectiveness of the City's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over financial reporting.

A deficiency in internal control over financial reporting exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control over financial reporting that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant

deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses. We identified certain deficiencies in internal control over financial reporting, described in the accompanying Schedule of Findings and Questioned Costs as items 2023-001 and 2023-002 that we consider to be significant deficiencies.

Report on Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City of Duluth’s financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the financial statements. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Minnesota Legal Compliance

In connection with our audit, nothing came to our attention that caused us to believe that the City of Duluth failed to comply with the provisions of the contracting – bid laws, depositories of public funds and public investments, conflicts of interest, public indebtedness, claims and disbursements, miscellaneous provisions, and tax increment financing sections of the *Minnesota Legal Compliance Audit Guide for Cities*, promulgated by the State Auditor pursuant to Minn. Stat. § 6.65, insofar as they relate to accounting matters. However, our audit was not directed primarily toward obtaining knowledge of such noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding the City’s noncompliance with the above referenced provisions, insofar as they relate to accounting matters.

The City of Duluth’s Response to Findings

Government Auditing Standards requires the auditor to perform limited procedures on the City of Duluth’s response to the findings identified in our audit and described in the accompanying Schedule of Findings and Questioned Costs and Corrective Action Plan. The City’s response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of This Report

The purpose of this report is solely to describe the scope of our testing of internal control over financial reporting and compliance, and the provisions of the *Minnesota Legal Compliance Audit Guide for Cities* and the results of that testing, and not to provide an opinion on the effectiveness of the City’s internal control over financial reporting or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City’s internal control over financial reporting and compliance. Accordingly, this communication is not suitable for any other purpose.

/s/Julie Blaha

Julie Blaha
State Auditor

June 20, 2024

/s/Chad Struss

Chad Struss, CPA
Deputy State Auditor



**Report on Compliance for Each Major Federal Program and Report on Internal
Control Over Compliance Required by the Uniform Guidance**

Independent Auditor's Report

The Honorable Roger Reinert, Mayor,
and Members of the City Council
City of Duluth, Minnesota

Report on Compliance for Each Major Federal Program

Opinion on Each Major Federal Program

We have audited the City of Duluth's compliance with the types of compliance requirements identified as subject to audit in the U.S. Office of Management and Budget (OMB) *Compliance Supplement* that could have a direct and material effect on each of the City of Duluth's major federal programs for the year ended December 31, 2023. The City of Duluth's major federal programs are identified in the Summary of Auditor's Results section of the accompanying Schedule of Findings and Questioned Costs.

In our opinion, the City of Duluth complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended December 31, 2023.

Basis for Opinion on Each Major Federal Program

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Our responsibilities under those standards and the Uniform Guidance are further described in the Auditor's Responsibilities for the Audit of Compliance section of our report.

We are required to be independent of the City of Duluth and to meet our other ethical responsibilities, in accordance with relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion on compliance for each major federal program. Our audit does not provide a legal determination of the City of Duluth's compliance with the compliance requirements referred to above.

Other Matter – Federal Expenditure Not Included in the Compliance Audit

The City of Duluth's basic financial statements include the operations of the Duluth Airport Authority and the Duluth Transit Authority, which expended \$14,571,892 and \$16,496,574, respectively, in federal awards which are not included in the City of Duluth's Schedule of Expenditures of Federal Awards during the year ended December 31, 2023. Our compliance audit, described in the Opinion on Each Major Federal Program section, does not include the operations of the Duluth Airport Authority and Duluth Transit Authority because they had separate single audits performed in accordance with the Uniform Guidance.

Responsibilities of Management for Compliance

Management is responsible for compliance with the requirements referred to above and for the design, implementation, and maintenance of effective internal control over compliance with the requirements of laws, statutes, regulations, rules and provisions of contracts or grant agreements applicable to the City of Duluth's federal programs.

Auditor's Responsibilities for the Audit of Compliance

Our objectives are to obtain reasonable assurance about whether material noncompliance with the compliance requirements referred to above occurred, whether due to fraud or error, and express an opinion on the City of Duluth's compliance based on our audit. Reasonable assurance is a high level of assurance but is not absolute assurance and, therefore, is not a guarantee that an audit conducted in accordance with auditing standards generally accepted in the United States of America, *Government Auditing Standards*, and the Uniform Guidance will always detect material noncompliance when it exists. The risk of not detecting material noncompliance resulting from fraud is higher than for that resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Noncompliance with the compliance requirements referred to above is considered material, if there is a substantial likelihood that, individually or in the aggregate, it would influence the judgment made by a reasonable user of the report on compliance about the City of Duluth's compliance with the requirements of each major federal program as a whole.

In performing an audit in accordance with auditing standards generally accepted in the United States of America, *Government Auditing Standards*, and the Uniform Guidance, we:

- exercise professional judgment and maintain professional skepticism throughout the audit;
- identify and assess the risks of material noncompliance, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the City of Duluth's compliance with the compliance requirements referred to above and performing such other procedures as we considered necessary in the circumstances; and
- obtain an understanding of the City of Duluth's internal control over compliance relevant to the audit in order to design audit procedures that are appropriate in the circumstances, and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of the City of Duluth's internal control over compliance. Accordingly, no such opinion is expressed.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and any significant deficiencies and material weaknesses in internal control over compliance that we identified during the audit.

Report on Internal Control Over Compliance

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the Auditor's Responsibilities for the Audit of Compliance section above and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies in internal control over compliance. Given these limitations, during our audit we did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above. However, material weaknesses or significant deficiencies in internal control over compliance may exist that were not identified.

Our audit was not designed for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, no such opinion is expressed.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

/s/Julie Blaha

Julie Blaha
State Auditor

June 20, 2024

/s/Chad Struss

Chad Struss, CPA
Deputy State Auditor

City of Duluth Duluth, Minnesota

Schedule of Findings and Questioned Costs For the Year Ended December 31, 2023

Section I – Summary of Auditor’s Results

Financial Statements

Type of report the auditor issued on whether the financial statements audited were prepared in accordance with generally accepted accounting principles: **Unmodified**

Internal control over financial reporting:

- Material weaknesses identified? **No**
- Significant deficiencies identified? **Yes**

Noncompliance material to the financial statements noted? **No**

Federal Awards

Internal control over major federal programs:

- Material weaknesses identified? **No**
- Significant deficiencies identified? **None reported**

Type of auditor’s report issued on compliance for major federal programs: **Unmodified**

Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)? **No**

Identification of major federal programs:

Assistance Listing Number	Name of Federal Program or Cluster
11.307	Economic Adjustment Assistance
21.027	COVID-19 – Coronavirus State and Local Fiscal Recovery Funds

Dollar threshold used to distinguish between Type A and Type B programs: \$1,010,177.

The City of Duluth qualified as a low-risk auditee? **Yes**

Section II – Financial Statement Findings

2023-001 **Access to Computer Systems/Network**

Prior Year Finding Number: N/A

Year of Finding Origination: 2023

Type of Finding: Internal Control Over Financial Reporting

Severity of Deficiency: Significant Deficiency

Criteria: When employees leave City employment, their access to the City’s various computer systems and network should be removed in a timely manner. It is the City’s policy to fully remove or disable access at the time of departure.

City of Duluth

Duluth, Minnesota

Condition: The City's Information Technology (IT) Department did not remove or disable access timely in all instances of City employees leaving employment tested.

Context: Twenty-five employees leaving City employment in 2023 were tested for timely removal of various systems, network, and/or data access. Six instances were identified where access had not been disabled or removed in a timely manner. In five of the six instances, employees' supervisors did not notify IT timely.

Effect: When terminated employees have access to the City's various computer systems, network, and data, it increases the risk that malicious damage to that information, fraud, and/or misstatements may occur.

Cause: The City does not have a formal policy in place that requires supervisors to timely notify IT of an employee's termination.

Recommendation: We recommend the City implement procedures to ensure the removal of terminated employees' computer system and network access in a timely manner.

View of Responsible Official: Acknowledge

2023-002 Key Card Access to Inventory Warehouse

Prior Year Finding Number: N/A

Year of Finding Origination: 2023

Type of Finding: Internal Control Over Financial Reporting

Severity of Deficiency: Significant Deficiency

Criteria: When employees leave City employment, their key card access to the City's various buildings/facilities should be removed in a timely manner. It is the City's policy to fully remove or disable key card access at the time of departure.

Condition: The City's Property Maintenance Department did not remove or disable access to the Inventory Warehouse in a timely manner in all instances of City employees leaving employment tested, or there was no audit trail documenting the removal.

Context: Nine of the 37 employees included on the access system list for the Inventory Warehouse were terminated employees.

Effect: When terminated employees have access to the City's buildings/facilities, it increases the risk that malicious damage to City information, fraud, and/or theft may occur.

Cause: The City's key card access system does not maintain documentation when an employee's key card access is removed.

Recommendation: We recommend the City implement procedures to ensure the removal of terminated employees' building/facility access is completed at the time of departure and documentation of the removal is maintained.

View of Responsible Official: Acknowledge

**City of Duluth
Duluth, Minnesota**

Section III – Federal Award Findings and Questioned Costs

No matters were reported.



City of Duluth
411 West First Street
Duluth, Minnesota 55802

218-730-5000
info@duluthmn.gov

Representation of City of Duluth Duluth, Minnesota

Corrective Action Plan
For the Year Ended December 31, 2023

Finding Number: 2023-001

Finding Title: Access to Computer Systems/Network

Name of Contact Person Responsible for Corrective Action: Ben VanTassel, Director of Administrative Services

Corrective Action Planned: Immediately, all supervisory staff will be reminded of the requirement to exit employees via the established process (Employee Exit Form) ahead of or on their exit date, which notifies applicable divisions of exiting employees and ensures employee's access to computer systems and network is removed. In addition, redundancies will be put in place within the Human Resources Division to follow up and verify that the established process has been followed. The City will develop and implement a policy/procedure for handling onboarding and exiting employees which sets forth the roles and responsibilities of all involved in the process.

Anticipated Completion Date: July 31, 2024

Finding Number: 2023-002

Finding Title: Key Card Access to Inventory Warehouse

Name of Contact Person Responsible for Corrective Action: Erik Birkeland, Property and Facilities Manager

Corrective Action Planned:

- PFM (Property and Facilities Management) is undertaking a complete internal audit of key card access for City staff in our card access system, and will be adjusting access as necessary based on findings.
- PFM is working with KFI Engineering to design and source a new key card access system for City Hall that will provide more controls and analytics to support complete documentation of activations and deactivations of City staff access, and will begin implementing this system as budgets allow in 2025.

- PFM is working with IT to develop a notification work order system that documents when the card access for an employee is requested and when it is terminated, and that will continue to remind staff to close the work order until it is complete while tracking all action taken to address the request.
- PFM is working on policies and procedures for timely notification of PFM staff when access needs to be terminated, and will coordinate these efforts with City Administration, HR, IT and the police department.
- PFM is working to refine access protocols and types of access for all areas, but specifically in to sensitive areas by using BCA compliance (finger printing, FBI background checks, etc.) for staff and contractors that need access to said spaces – this effort has been underway for 7 years and continues to be refined.
- PFM is currently ensuring that all door access for former employees is not only unchecked (in the current archaic system) but that all individual door access is removed as well – this is a glitch in the current system that allows PFM to cut off the main access to all areas, but access still shows up in the system at the individual door level even though access has been terminated.
- PFM is manually recording the date and time employee access has been requested and terminated, and will continue to do so until the new card access system is implemented and this data becomes integral to the use of the new system.
- PFM is facilitating a security analysis study with a third-party consultancy (Guideposts) to assess security and access controls, policies, physical design characteristics and procedures in City Hall. Once the study is complete, PFM will work with Administration to implement the recommendations at Administration’s discretion.
- PFM is developing redundancies in the staffing of key card access management, and will be moving from having one staff member managing this system to have 2-3 staff members managing the system to account for vacations and sick leave causing delays to implementation.
- PFM is working with Administration to develop access protocols and permission levels for sensitive areas (such as Finance).

Anticipated Completion Date:

1. New Key Card System in City Hall – anticipate having it installed and operational by the end of 2025 by utilizing 2025 CIP funding to cover the costs of implementation.
2. Internal work order system to track and manage timely removal of key card access – anticipate having this in place within the next 2-3 months – will document this work manually until a new internal system is in place.
3. Policies and procedures for key card access termination for the City organization (i.e. notification of PFM and PFM responsibilities, etc.) – anticipate this will be complete and implemented within the next 2-3 months.
4. Security study of City Hall – this work is nearly complete, and based on the recommendations and directives of Administration, implementation is likely to begin within 2-3 months and will proceed to completion as funding allows with a likely completion date at the end of 2025.
5. Policies and procedures for access to sensitive areas by City staff – anticipate having these policies and procedures in place within 2-3 months, but PFM is currently operating under a working set of protocols to better track and manage current access to sensitive areas in the meantime.
6. Work on BCA compliance for appropriate City staff and contractors is underway and will continue to be refined going forward so that maintenance, project and IT work can proceed in these areas.
7. PFM internal access audit of City staff key card access will be complete within the next 1-2 months.

**Duluth Economic Development Authority
Management and Compliance Report
Year Ended December 31, 2023**



**Report on Internal Control Over Financial Reporting and on Compliance and
Other Matters Based on an Audit of Financial Statements Performed in
Accordance with *Government Auditing Standards***

Independent Auditor's Report

Board of Commissioners
Duluth Economic Development Authority
Duluth, Minnesota

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the City of Duluth, Minnesota, which include as Supplementary Information, the financial statements of the Duluth Economic Development Authority, a discretely presented component unit, as of and for the year ended December 31, 2023, and the related notes to the financial statements, which collectively comprise the City's basic financial statements, and have issued our report thereon dated June 20, 2024.

Report on Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Duluth Economic Development Authority's internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing our opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control over financial reporting.

A deficiency in internal control over financial reporting exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control over financial reporting that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses. However, material weaknesses or significant deficiencies may exist that were not identified.

Report on Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Duluth Economic Development Authority's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material

effect on the financial statements. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Minnesota Legal Compliance

In connection with our audit, nothing came to our attention that caused us to believe that the Duluth Economic Development Authority failed to comply with the provisions of the contracting – bid laws, depositories of public funds and public investments, conflicts of interest, claims and disbursements, miscellaneous provisions, and tax increment financing sections of the *Minnesota Legal Compliance Audit Guide for Cities*, promulgated by the State Auditor pursuant to Minn. Stat. § 6.65, insofar as they relate to accounting matters. However, our audit was not directed primarily toward obtaining knowledge of such noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding the Authority’s noncompliance with the above referenced provisions, insofar as they relate to accounting matters.

Purpose of This Report

The purpose of this report is solely to describe the scope of our testing of internal control over financial reporting and compliance, and the provisions of the *Minnesota Legal Compliance Audit Guide for Cities* and the results of that testing, and not to provide an opinion on the effectiveness of the Authority’s internal control over financial reporting or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority’s internal control over financial reporting and compliance. Accordingly, this communication is not suitable for any other purpose.

/s/Julie Blaha

Julie Blaha
State Auditor

June 20, 2024

/s/Chad Struss

Chad Struss, CPA
Deputy State Auditor