March 21, 2012

The Honorable Theo Beckmann  
Mayor, City of Freeborn  
P.O. Box 151  
Freeborn, Minnesota 56032-0151

The Honorable Steve Ausen  
Chair, Town of Freeborn Board of Supervisors  
30085 - 670th Avenue  
Hartland, Minnesota 56042

Fire Chief and Ambulance Captain Steve Seipp  
Freeborn Fire Department  
P.O. Box 108  
Freeborn, Minnesota 56032-0108

Dear Mayor Beckmann, Chair Ausen, and Fire Chief Seipp:

Since at least 2007, the audits for the City of Freeborn (“City”) have contained a finding that the Freeborn Fire Department (“Fire Department”) maintained its own financial accounts. The Office of the State Auditor (“OSA”) reviewed the handling of Fire Department funds. The OSA found that Fire Department funds were not handled in accordance with applicable joint powers agreements or Minnesota law.

This letter will provide the City, the Town of Freeborn (“Town”), and the Fire Department with guidance to bring the handling of Fire Department funds into compliance with Minnesota law. The OSA also requests that the City and Town notify the OSA of the steps that have been taken to resolve these issues.

Background

The City and the Town entered into a Joint Powers Agreement dated June 14, 1999, ("1999 Agreement") “to jointly construct and operate a municipal building (the ‘facility’) and associated fire-fighting and emergency vehicles and equipment (the ‘equipment’).”

1 See 1999 Agreement, section 1. Both parties agreed that the facility would house fire-fighting equipment and ambulances owned by either or both of the parties, provide cleanup facilities for the fire department and ambulance services operated jointly by the City and Town, serve as the City and Town municipal
Under the 1999 Agreement, the City and the Town jointly owned the facility and all equipment, including equipment previously titled in the name of either of the parties. The 1999 Agreement established a “facility operating committee” consisting of the City’s Mayor and the Town’s Board Chair. This committee made recommendations to the City Council about the operation and maintenance of the facility and equipment. However, the City Council had to authorize all expenditures and contracts, including expenditures for the maintenance, repair and replacement of equipment, and the City was responsible for accounting for costs. The Town agreed to reimburse the City 50% of the costs.

On November 13, 2008, the City and Town entered into another Joint Powers Agreement (“2008 Agreement”). After referencing the 1999 Agreement, the 2008 Agreement stated that the City and Town wanted to establish an Operating Board (“Board”) to oversee the operation of the Fire Department. The Board was to be comprised of two members appointed by the City, two members appointed by the Town, and one member elected by the members of the Fire Department. The Board was given the “exclusive authority” to manage the operation, spending, and activity of the Fire Department. While the Board was required to appoint a Treasurer from the Fire Department’s membership “to manage and maintain” the Fire Department’s financial activities, all expenditures had to be approved by a 4 out of 5 vote of the Board. The 2008 Agreement provided that funding for the Board’s expenditures would be split 50-50 between the City and the Town.

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1 See 1999 Agreement, paragraphs 2.1, 2.2, and 5.9.
2 See 1999 Agreement, paragraph 5.1.
3 See 1999 Agreement, paragraphs 5.1 and 5.9. The 1999 Agreement expressly provided that the committee was not a joint powers board with the power to issue bonds, obligations or other forms of indebtedness under Minn. Stat. § 471.59 (11). See 1999 Agreement paragraph 5.1.
4 See 1999 Agreement, paragraphs 5.1, 5.4, and 5.9. The City and Town were to jointly approve an annual budget for the costs. See 1999 Agreement, paragraph 5.4.
5 See 2008 Agreement, art. I.A. The Board was required to conduct meetings in compliance with the Minnesota Open Meeting Law. See 2008 Agreement, art. II.C.
6 See 2008 Agreement, art. II.A. The Board was also granted the authority to enter into contracts, borrow funds, apply for grants, and approve payments for claims. See 2008 Agreement, art. IV.A.
7 See 2008 Agreement, art. III.B. The 2008 Agreement also acknowledged that the State Auditor had the authority to examine and audit documents involving transactions related to the 2008 Agreement. See 2008 Agreement, art. VI.
8 See 2008 Agreement, art. III.A.
On November 14, 2011, the Board voted in a 4 to 1 vote to disband. Upon dissolution, the 2008 Agreement required an accounting to determine the assets and liabilities of the Board. The 2008 Agreement also required the liquidation of the Board’s assets, and the distribution of the liquidated proceeds, after payment of liabilities, to the City and Town, in proportion to their contributions.

Fire Department Accounts

There is no fire relief association directly associated with the Fire Department. Therefore, there are no fire relief association accounts.

According to the Fire Chief, the Fire Department maintained two accounts that were City accounts. According to the Fire Chief:

- One account (“Account #1”) contained funds from fire service contracts, fire call payments, grants, and donations from the “Freeborn Fire Fund.” The account was used to pay operating expenses of the department such as training, equipment, repairs, and fuel. The OSA was provided with a Financial Report dated December 5, 2011, for activity since November 7, 2011. It reported that Account #1 had an ending balance of $22,824.93.
- Another account contained State Fire Aid (“State Fire Aid Account”). While the account had been used to pay for firefighting equipment, the funds had been “encumbered” to start a relief association for the Fire Department members. The Fire Department Financial Report dated December 5, 2011, reported $5,926.61 as the ending balance in this account.

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12 See Operating Board Minutes (November 14, 2011); see also City Council Meeting Minutes (December 13, 2011).
13 See 2008 Agreement, art. VII.B (dissolution by a 4 of 5 vote of the Board).
14 Id. Minnesota law requires a joint powers agreement to provide for the disposition of any property acquired as a result of the joint powers agreement. See Minn. Stat. § 471.59, subd. 5. In addition, any surplus moneys must be returned to the contracting parties in proportion to the contributions of the contracting parties. Id.
15 The December 13, 2011, City Council meeting minutes reported that the Fire Department was looking into setting up a Relief Association.
16 The two accounts appear to be reported in the City’s audits as part of the City’s Fire Fund, a Special Revenue Fund. It is the OSA’s understanding that the Fire Department continues to maintain these accounts.
17 The OSA was provided with copies of fire service contracts between the City and the Townships of Carlston and Manchester dated March 10, 2009, and covering the time period of April 1, 2009, through March 31, 2014.
18 The City Clerk/Treasurer confirmed that the Fire Department issues checks for fuel, maintenance on vehicles, equipment, and miscellaneous items. According to the City Clerk/Treasurer, the City and Town split the costs for utilities, telephone, insurance, fire truck bonds, and building maintenance.
19 This amount agrees with the balance reported to the OSA’s Pension Division on the City’s annual reporting form.
Checks from the two accounts were approved by the Fire Department members, and signed by a member of the City Council and a Town Board supervisor.\textsuperscript{20}

The Fire Chief also reported that the Ambulance Secretary maintained control of an Ambulance checking account and an Ambulance savings account, consisting of money from call fees and donations.\textsuperscript{21} The checks from the Ambulance account are also signed by the member of the City Council and the Town Board supervisor. According to the Fire Chief, the Ambulance accounts were used to pay Ambulance expenses such as equipment, training, and repairs. The OSA was provided with a hand-written document that appears to report a November 30, 2011, balance of $12,267.89 in the checking account and $6,654.17 in the savings account. The document also listed $4,405 in “December bills,” including $55.00 for two fruit baskets.

Finally, the Fire Chief reported that the Fire Department maintained a “Freeborn Fire Fund,” which he described as the Fire Department’s fundraising and donation account. According to the Fire Chief, the account was managed by the Fire Department Treasurer, and disbursements from the account were reported on monthly financial reports approved by Fire Department members.

The Fire Chief reported that the Freeborn Fire Fund was used to purchase equipment and to handle Fire Department expenses “not payable out of the other two accounts.” The Financial Report dated December 5, 2011, for activity since November 7, 2011, reported that the “Firefighters’ Fund,” which appears to be the Freeborn Fire Fund, had deposits of $11,940, resulting in an ending balance of $22,668.10. Included among the $1,543.42 in reported expenses on the Financial Report were: $559.85 for a “FFR dinner,” $67.70 for “Nov. supper,” and $50.00 for “FFR gambling license.” In February 2012, the OSA was informed that the account was used for a $540 “gift” to a retired firefighter.

\textbf{Nonprofit “Freeborn Fire Department”}

On October 7, 2009, Articles of Incorporation were filed with the Minnesota Secretary of State for the “Freeborn Fire Department,” a nonprofit corporation. The Fire Chief is listed as the incorporator of the nonprofit.

\textsuperscript{20} The OSA was informed that this check signing procedure was used both when the Board was in place and after the Board disbanded. However, the Fire Department Constitution and By Laws that appear to have been approved by the Board at a June 15, 2009, meeting state that Fire Department checks were to be signed by the Fire Chief and Fire Treasurer, and checks related to ambulance personnel were to be signed by the Ambulance Captain and Ambulance Secretary/Treasurer, “per written financial policy.” \textit{See} Constitution and By-Laws of the Freeborn Volunteer Fire and Ambulance Department, Art. 3, sections 6 and 8. Furthermore, the Fire Chief reported at a March 18, 2009, Board meeting that he and the Fire Department’s Secretary/Treasurer were paying the Fire Department’s bills. \textit{See} Board Meeting Minutes (March 18, 2009).

\textsuperscript{21} According to the Fire Chief, the Ambulance Secretary makes deposits into the accounts, writes checks from the checking account, receives bank statements, balances the accounts, and provides a monthly financial report for approval by Ambulance members, the City and the Town.
Recommendations

The OSA reviewed the handling of Fire Department funds. The OSA found that Fire Department funds were not handled in accordance with applicable joint powers agreements or Minnesota law.

Based upon its review, the OSA makes the following recommendations:

1) Public Funds Must Be Controlled by the City, Town or a Joint Powers Entity

Minnesota law requires city councils and town boards to have full control over their municipality’s financial matters.\(^{22}\) City funds may be paid only upon an order drawn by the mayor, the city clerk, and the city treasurer; town funds may be paid only on an order of the town board, signed by the chair, clerk and treasurer.\(^{23}\) Furthermore, the underlying claims for disbursements of city or town funds must be reviewed and allowed by the city council or town board before the actual disbursements are made.\(^{24}\) These controls apply to all city and/or town departments, including a fire department.\(^{25}\)

Under Minnesota law, the disbursement of funds by a joint powers entity must “agree as far as practicable with the method provided by law for the disbursement of funds by the parties to the agreement.”\(^{26}\) Similarly, contracts let and purchases made under a joint powers agreement must conform to the requirements applicable to contracts and purchases of any one of the parties to the agreement.\(^{27}\) All expenditures of public funds must be based on specific authorization for the expenditure and must be for a public purpose.\(^{28}\)

Under the 2008 Agreement, four of the five members on the Board needed to approve all expenditures. Under the 1999 Agreement, the City Council needed to approve all expenditures. Neither Agreement allowed the members of the Fire Department to approve the expenditure of public funds.

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\(^{22}\) See Minn. Stat §§ 366.01, subd. 1 (towns), and 412.241 (cities).

\(^{23}\) See Minn. Stat §§ 367.18 (towns), 412.14, and 412.271, subd. 1 (cities).

\(^{24}\) See Minn. Stat. §§ 367.18 (towns), 412.271, subd. 1 (cities), and 471.38 (towns and cities).

\(^{25}\) Further guidance on this issue is found in the OSA’s Statement of Position on Fire Departments, Fire Relief Associations and Checking Accounts. The OSA’s Statements of Position are available on the OSA’s website, www.auditor.state.mn.us. The City’s auditors previously provided the City with a copy of one of the OSA’s Fire Department Statements of Position. See Letter to Freeborn City Council from Hill, Larson, Walth & Benda, P.A. (August 6, 2010), part of the City’s 2009 audit.

\(^{26}\) See Minn. Stat. § 471.59, subd. 3. Minnesota law also requires joint powers entities to provide for “[s]trict accountability of all funds” and reports of all receipts and disbursements. Id.

\(^{27}\) See Minn. Stat. § 471.59, subd. 3. The City’s auditors reported that the City did not comply with Minnesota’s contracting and bidding requirements when it purchased fire equipment for over $25,000 in 2010 without considering the State’s cooperative purchasing venture before making the purchase. See Independent Auditor’s Report on Minnesota Legal Compliance (June 8, 2011).

\(^{28}\) Additional guidance on the public purpose doctrine is found in the OSA’s Statement of Position on Public Expenditures: Donations and Dues.
a) Fire Department Account #1 and the Ambulance Accounts

The Fire Department’s Account #1 and the Ambulance accounts are comprised of public funds. These public funds must be controlled by the City, the Town, or a joint powers entity. There must be specific authority and a public purpose for all expenditures. Because there is no longer a joint powers entity, the OSA recommends that the funds be turned over to the City, consistent with the 1999 Agreement.

b) The State Fire Aid Account

There is no relief association directly associated with the Fire Department. The City receives state fire aid, but turns the money over to the Fire Department within 30 days of receipt.

Under Minnesota law, state fire aid received by a municipality with no relief association directly associated with the municipality’s fire department must be deposited in a special account for that purpose in the municipal treasury. The municipality may only use the funds for the payment of:

1) Certain fees, dues and assessments;
2) The cost of purchasing and maintaining needed fire department equipment; and
3) The cost of construction, acquisition, repair, or maintenance of buildings or other premises to house fire department equipment.

29 The Ambulance-related vehicles and equipment are part of the Fire Department. See, e.g., 1999 Agreement, section 1; Minutes of the Joint Meeting – Freeborn Township and City of Freeborn (September 2, 2008); Minutes of the Operating Board Meeting (March 18, 2009).
30 The OSA questions the authority to use Ambulance funds to purchase fruit baskets.
31 The accounts should reflect the City’s tax identification number, and signature cards for the accounts should contain the authorized City signatures. It is a crime to intentionally refuse or omit to pay over to a political subdivision money received on behalf of or for the account of the political subdivision. See Minn. Stat. § 609.445. Suggestions that the Health Insurance Portability and Accountability Act (“HIPAA”) may somehow prevent the City from controlling the Ambulance funds are unfounded; the City would need to comply with any HIPAA-related requirements.
32 The State Fire Aid is reported in the City’s audits as part of the Fire Fund (a Special Revenue Fund). For 2007 through 2011, the City received the following state fire aid: 2011 - $4,050; 2010 - $4,101; 2009 - $3,594; 2008 - $4,117; and 2007 - $4,829. The annual reporting forms for municipalities without relief associations submitted by the City to the OSA’s Pension Division report that part of the state fire aid received was expended on equipment purchases and/or maintenance, leaving a balance of $5,926.61 in the restricted fire fund as of December 31, 2011.
33 See Minn. Stat. §424A.08. The statute provides exceptions if certain firefighters are covered by other retirement plans.
34 See Minn. Stat. §424A.08.
The OSA knows of no authority for the City to pay state fire aid to the Fire Department. Furthermore, the Fire Chief reported that state fire aid has been “encumbered” to start a relief association. The OSA knows of no authority that would allow anyone to encumber state fire aid to start a relief association.

The OSA recommends that the state fire aid account be turned over to the City, in compliance with Minnesota law.

c) The “Freeborn Fire Fund”

The Fire Chief described the Freeborn Fire Fund as the Fire Department’s fundraising and donation account.

Donations to a city or town fire department are actually donations to the city or town, with limitations on the way the donated funds may be used. A city council or town board may accept gifts for its fire department in accordance with the terms prescribed by the donor. However, under Minnesota law, the gifts must be accepted by a resolution approved by a two-thirds majority of the governing body.

A city or town fire department does not have the authority to accept gifts for the fire department. If members of a fire department or a separate nonprofit corporation wish to hold fundraising events for the fire department, the funds raised must be donated to the city or town. All fundraising materials should clearly designate that such fundraising events are being held by members of the fire department or a separate nonprofit corporation, not the fire department itself, the city, or the town. In turn, the city or town must comply with Minnesota law when accepting the donation. All donations accepted by the City or Town become public funds and must be expended only for public purposes.

The expenditures from the Freeborn Fire Fund included dinners and a gambling license. It is questionable whether public funds could be used for these expenditures. Generally,

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35 If a city has a relief association related to its fire department, Minnesota law requires a city treasurer to transfer state fire received by a city to the relief association’s treasurer within 30 days of receipt. See Minn. Stat. § 69.031, subd. 5(a). The fire aid must be deposited in the relief association’s special fund, which is the relief association’s restricted pension fund. See Minn. Stat. § 424A.05, subd. 2.
36 See Fire Chief and Ambulance Captain Steve Seipp’s Response/Reply to Fire Department Funds Accounts (undated; received by the OSA in February 2012).
37 See Minn. Stat § 465.03 (2010). Any conditions placed on the use of the gift must be fully described in the resolution.
38 Further guidance on this issue is found in the OSA’s Statement of Position on Fire Departments and Fire Relief Association Fundraisers and Donations.
39 Cities and towns may not simply provide dinners to employees or volunteers. See OSA’s Statement of Position on Employee Recognition Programs and Events. Town electors may set an amount at the town’s annual meeting or a special meeting to spend to recognize volunteers and service efforts. See Minn. Stat. § 365.10, subs. 1 and 12. Cities may establish a program of preventive health and employee recognition services. See Minn. Stat. § 15.46.
these types of expenditures are made from a fire relief association’s general fund, if authorized in the association’s articles of incorporation or by-laws. However, there is no relief association directly associated with the Fire Department.

If the “gift” to a retired firefighter paid from the Freeborn Fire Fund was actually a form of a pension payment, such a payment would generally fall under the rules adopted by a fire relief association for payments from the association’s special (pension) fund. However, there is no relief association directly associated with the Fire Department. Cities and towns have no authority to provide an individual with a “gift” of public funds.

It appears the funds in the Freeborn Fire Fund were raised for the Fire Department. Therefore, the OSA recommends that the funds be transferred to the City or Town, and accepted by the City or Town as required by law. Once donated to the City or Town, there must be specific authority for the expenditure of the funds, and the funds may only be used for a public purpose. In the future, the OSA recommends that all fund-raising events clearly designate for whom the funds are being raised.

2) The City and Town Should Adopt an Agreement That Accurately Describes Their Relationship with the Fire Department

The City and Town share ownership of the Fire Department and Ambulance vehicles, equipment, and facility. Without a joint powers board, either the City or the Town should be responsible for approving all disbursements of Fire Department funds and all contracts involving the Fire Department, as required by Minnesota law.

The OSA recommends that the City and Town work with their attorneys, the League of Minnesota Cities, and/or the Minnesota Association of Townships to draft an agreement that accurately reflects how the City and Town will be operating the Fire Department in the future. For additional guidance on this issue, a copy of the State Auditor’s article “Joint Powers Fire Departments and Fire Districts: What You Need To Know” is enclosed.

Once the City and Town enter into a new Fire Department joint powers agreement, the agreement should be reviewed on a regular basis and revised when actual practice no longer follows the terms of the agreement.

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40 See Minn. Stat. § 424A.06. See also OSA’s Statement of Position on Fire Relief Association Funds: Special and General Funds, and Charitable Gambling Funds.
41 See OSA’s Statement of Position on Fire Relief Association Funds: Special and General Funds, and Charitable Gambling Funds.
42 See OSA’s Statement of Position on Public Expenditures: Donations and Dues.
43 See OSA’s Statement of Position on Public Expenditures: Donations and Dues.
44 See also the League of Minnesota Cities (LMC) publications on “Ten Things to Watch for When Entering Into Joint Powers Agreements” and “Fire Service Contracts: Can You Put That In Writing?”, available on the LMC’s website, www.lmc.org.
3) The Status of the Nonprofit “Freeborn Fire Department” Should be Resolved

The relationship of the nonprofit “Freeborn Fire Department” corporation to the Fire Department is unclear.\(^{45}\)

The Fire Department has been operating as a fire department affiliated with a municipality, not as an independent nonprofit fire-fighting corporation. Under the joint powers agreements, the City and Town, not a nonprofit corporation, own the vehicles, equipment, and facility. Under the joint powers agreements, the City or the joint powers board, not a nonprofit corporation, operate the Fire Department. Under the joint powers agreements, the City and the Town, not a nonprofit corporation, split the costs of operating the Fire Department. Furthermore, the fire service contracts with the Townships of Carlston and Manchester are with the City, not with a nonprofit corporation.

While a joint powers entity may incorporate itself as a nonprofit, the OSA found no evidence in the Board’s meeting minutes that the Board authorized any such incorporation.\(^{46}\) More importantly, the joint powers agreements do not authorize the transformation of the Fire Department, an entity jointly owned and operated by the City and Town, into an independent nonprofit firefighting corporation. The OSA knows of no authority for a nonprofit corporation to assert control over City and Town assets.

The status of the nonprofit “Freeborn Fire Department” corporation should be resolved. It appears to the OSA that the nonprofit corporation should be dissolved.

4) The City and Town Must Maintain Copies of Public Records

In the City’s 2009 and 2010 audits, the City’s auditors stated that they were unable to obtain a signed copy of the joint powers agreement establishing the joint powers board (the 2008 Agreement). In addition, the City’s auditors reported in the City’s 2008 and 2010 audits that invoices for some Fire Department disbursements were missing.

Minnesota’s record retention laws require public entities to “make and preserve all records necessary to a full and accurate knowledge of their official activities.”\(^{47}\) In

\(^{45}\) As stated previously in this letter, Articles of Incorporation for the nonprofit were filed with the Minnesota Secretary of State in 2009, with the Fire Chief listed as the incorporator of the nonprofit.

\(^{46}\) See Minn. Stat. § 465.717 (a joint powers entity may not create a nonprofit corporation unless explicitly authorized to do so by law; a joint powers entity that incorporates itself as a nonprofit must comply with all laws applicable to the participating political subdivisions and shall possess only the authority that the joint powers entity possessed). Although the OSA requested and reviewed copies of the Operating Board’s meeting minutes, the minutes provided to the OSA do not appear to be a complete set. For example, the OSA received no minutes from 2010.

\(^{47}\) See Minn. Stat. § 15.17, subd. 1. See also Minn. Stat. ch. 13 (Minnesota Government Data Practices Act) and Minn. Stat. § 138.17 (government records).
addition, the 2008 Agreement required the joint powers entity to maintain documents for six years from the date the 2008 Agreement was terminated. All public records must be delivered to the record custodian’s successor.

We recommend that the City, the Town, and any joint powers entity created by the City and Town, retain records in compliance with Minnesota law. All Fire Department records should be delivered to the entity designated by the City and Town as custodian of the records.

5) Members of the Fire Department Should Decide Whether They Want a Fire Relief Association

If members of the Fire Department want to create a relief association, they should contact the OSA’s Pension Director Rose Hennessy Allen for further information and guidance at 651-296-5985 or through email at Rose.Hennessy-Allen@osa.state.mn.us. Members of the Fire Department may also want to review the Minnesota Public Employees Retirement Association’s (PERA) website, www.mnpera.org, regarding the steps firefighters would need to take to become members of PERA for pension purposes.

Conclusion

The OSA reviewed the handling of public Fire Department funds. The OSA found that Fire Department funds were not handled in accordance with applicable joint powers agreements or Minnesota law. Therefore, in compliance with Minn. Stat. §§ 6.50 and 6.51, a copy of this letter is being filed with the City Attorney, the Freeborn County Attorney, and the Freeborn County Auditor.

In this letter, the OSA has provided recommendations to bring the City, the Town, and the Fire Department’s finances into compliance with Minnesota law. By June 1, 2012, please provide us with a description of how these issues are being resolved. If you have any questions, please contact me at 651-297-5853 or through email at nancy.bode@osa.state.mn.us, or contact Kathy Docter at 651-282-2388 or through email at kathy.docter@osa.state.mn.us.

Sincerely,

/\ Nancy J. Bode

Nancy J. Bode
Assistant Legal Counsel

48 See 2008 Agreement, art. VI.
49 See Minn. Stat. § 15.17, subd. 3.
50 Any person who intentionally and unlawfully removes, mutilates, destroys, conceals, alters, defaces or obliterate a public record is guilty of a misdemeanor. See Minn. Stat. § 138.225.
Enclosure

cc: The Honorable Kaleb Bjornstad, Freeborn City Council
The Honorable James Beach, Freeborn City Council
The Honorable Edward Mosser, Freeborn City Council
The Honorable Patrick Stenzel, Freeborn City Council
Ms. Tiffany Krueger, City Clerk/Treasurer
Hill, Larson, Walth, and Benda, City Auditor
The Honorable Matthew Theede, Township Supervisor
The Honorable Al Hunnicutt, Township Supervisor
Ms. Tabetha Mithun, Township Clerk
Ms. Julie Stenzel, Township Treasurer
Ms. Rose Hennessy Allen, OSA Pension Director
Mr. Perry Berg, City Attorney
The Honorable Craig S. Nelson, Freeborn County Attorney
The Honorable Dennis Distad, Freeborn County Auditor-Treasurer