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STATE AUDITOR

August 19, 2003

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The Honorable Doug Keith
Mayor, City of Florence
RR 1 Box 26A
Florence, Minnesota 56170-9401

Dear Mayor Keith:

The Office of the State Auditor (OSA) completed an investigation regarding an alleged theft of City funds by Ms. Diane Wixon, a former Clerk/Treasurer of the City of Florence (City). The findings of our investigation, covering the time period January 1, 1999 through December 31, 2001, were forwarded to the Lyon County Attorney in an Investigative Report dated October 25, 2002. As you are aware, Ms. Wixon was charged in November 2002 with four counts of theft. At the Lyon County Attorney's request, we conducted a supplemental investigation for the time period April 1, 1996 through December 31, 1998. The findings of our supplemental investigation were forwarded to the Lyon County Attorney in a Supplemental Investigative Report dated March 5, 2003.

We understand that the criminal matter remains unresolved. However, rather than continuing to wait for a resolution of that matter, we want to share with you a number of weaknesses in the internal controls and management practices of the City that we identified based upon our review of documents obtained from the City's financial institution, and the limited number of City documents that the City could provide to us.¹ We understand the City has been working with the City Auditor to correct past management practices. The purpose of this letter is to report our findings, to make recommendations that will address the weaknesses identified, and to assist the City in further protecting its assets in the future.² This letter will address weaknesses in:

- The City's receipts and disbursements practices;
- The City's practices for maintaining City records; and
- The City's Financial Reporting Forms.

¹ We understand that the City engaged Meulebroeck, Taubert & Co., PLLP, certified public accountants, to conduct an audit for the City for the year ended December 31, 2001 and December 31, 2002. We also understand that the City has worked with Mr. Meulebroeck to improve the internal controls and management practices of the City. This letter is based upon practices that we observed during our investigation, and is limited to the time period April 1996 through December 2001.

² Copies of the public release of the October 25, 2002 and March 5, 2003 reports are enclosed with this letter. The public versions of the investigative reports may also be found on the OSA's website:
www.auditor.state.mn.us.

FINDINGS AND RECOMMENDATIONS

I. City Receipts and Disbursements Practices

A city council is responsible for city funds.³ City funds must only be disbursed after the claim for the funds has been reviewed and approved by the city council.⁴ During its review, the OSA found several instances where the City's practices did not meet statutory requirements for the maintenance, receipt and disbursement of City funds.

The OSA found that Certificates of Deposit belonging to the City appear to have been cashed, and the funds transferred to the City's General Account, without City Council authorization.⁵ The OSA was informed that the City's Mayor routinely pre-signed City checks.⁶ None of the City's checks contained a claim declaration, and it appears that the City did not require claimants to verify claims on a separate form.⁷ It appears that the Clerk/Treasurer did not prepare or submit a list of claims to the City Council for review before City checks were issued each month, and no references were included in City Council meeting minutes regarding which claims, if any, the City Council had authorized for payment.⁸ It appears that City bank statements were not

³ See Minn. Stat. § 412.241 (2002). A city treasurer must "receive and safely keep all moneys belonging to the city" and keep the funds of the city, as far as possible, in the depositories designated by the city. See Minn. Stat. §§ 412.141 and 427.03 (2002).

⁴ See Minn. Stat. §§ 412.271, subd. 1, and 412.141 (2002). No disbursement of city funds "shall be issued until the claim to which it relates has been audited and allowed by the council." Minn. Stat. § 412.271, subd. 1 (2002). It is the city treasurer's duty to promptly "enter in a book" an account of all moneys received and disbursed, including the "source and objects thereof" and the date of each transaction. Minn. Stat. § 412.141 (2002). It is the city clerk's duty to keep an account book reflecting all money transactions of the city, including the dates and amounts of all receipts, the person from whom money was received, and all orders drawn upon the treasurer with their payee and object. Minn. Stat. § 412.151, subd. 1 (2002). In cities with combined clerk-treasurer positions, the duties of the treasurer are to be performed by the clerk-treasurer. Minn. Stat. § 412.02, subd. 3 (2002). Generally, a city must not pay a claim until the claimant has signed a declaration stating that the claim is just, correct and no part of it has been paid. See Minn. Stat. § 471.38 (2002). As an alternative, a city may have a declaration statement printed on the reverse side of the city's checks. Minn. Stat. § 471.391, subd. 2 (2002). The necessary language for either type of declaration is set forth in Minn. Stat. § 471.391 (2002).

⁵ In addition, it appears that a Certificate of Deposit was purchased on behalf of the City without City Council authorization.

⁶ As recently as 2001, City checks had three signature lines for mayor, city clerk and city treasurer, even though the OSA was informed that the City combined the offices of city clerk and city treasurer in 1996. The OSA observed that most City checks contained three signatures: the Mayor, the City Clerk/Treasurer, and a City Council member. However, the OSA observed that at least one City check contained only two signatures.

⁷ See Minn. Stat. § 471.38 (2002).

⁸ The only claims lists provided to the OSA were for the months of March, May, June and July 2001.

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reconciled to the City's cash book balances on a regular basis. The OSA was informed that in 2001 at least one claim for \$251.00 was paid by the City in cash.⁹

During the OSA's period of review, the Clerk/Treasurer was responsible for receiving, recording, and depositing City funds, as well as preparing and issuing all City checks.¹⁰ While the concentration of duties and responsibilities in one individual is permitted under Minnesota law, it requires the city council to take a more active oversight role.

The OSA recommends that the City comply with Minnesota law. Specifically, the OSA recommends that the City implement the following receipting and disbursement procedures:

- City checks should not be pre-signed and must contain at least two signatures (mayor and clerk/treasurer);¹¹
- The City Clerk/Treasurer should use a ledger, specifying all receipts, disbursements, and transfers for all separate funds/accounts;
- City bank statements should be reconciled to the City's cashbook balances on a monthly basis;
- Claimants should be required to sign a claim declaration form;
- Each claim should be considered for payment during a City Council meeting;¹²
- Claims approved by the City Council for payment should be referenced in the meeting minutes, or in documentation attached to the minutes;¹³ and
- City claims should not be paid in cash.

The OSA also recommends the City's bank be provided with two signatures, or a copy of a City Council resolution, prior to any transfer of the City's Certificate of Deposit funds.

II. City Records

The OSA found that the City did not maintain records as required by law. Many City records could not be located during the OSA's investigation, and the OSA had to obtain the City's financial records directly from the City's financial institution.¹⁴ The OSA was informed that the

⁹ The City's Auditor informed the OSA that he had located approximately \$660.00 in undeposited water and garbage receipts for the year 2001. When the OSA began its investigation, the OSA was informed by the City's then Clerk/Treasurer that the receipt book for the water and garbage bills appeared to no longer exist.

¹⁰ It is unclear whether the City adopted an ordinance to combine the offices of Clerk/Treasurer as required by Minn. Stat. § 412.02, subd. 3 (2002). *See also* Minn. Stat. § 412.591, subd. 2 (2002). It is also the OSA's understanding that the City's Clerk/Treasurer was not bonded. *See* Minn. Stat. §§ 412.111 and 418.25 (2002) (cities may pay for bonds).

¹¹ Signature cards must be updated every time there is a change in authorized signers. *See* Minn. Stat. §§ 412.271, subd. 1, and 412.141 (2002).

¹² *See* Minn. Stat. § 412.271, subd. 1 (2002).

¹³ *See* Minn. Stat. § 412.151, subd. 1 (2002).

¹⁴ For example, the City did not maintain bank statements or copies of cancelled City checks. As a result, the OSA had to contact the City's bank to obtain copies of City documents. The OSA was informed that the City's

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former Clerk/Treasurer kept City records at her home and refused to provide the records to the City when she left the Clerk/Treasurer position.¹⁵

During its investigation, the OSA was provided with, and reviewed, the City Council meeting minutes for the year 2001. The OSA noted that individual votes of the Council members were not recorded in the minutes, and individual claims approved for payment were not itemized in the minutes.¹⁶

The OSA recommends that the City comply with Minnesota law. Specifically, the OSA recommends that the City:

- Maintain complete minutes of City Council meetings; and
- Maintain control of all City records.

III. City Financial Reporting Forms

The OSA reviewed Financial Reporting Forms filed by the City with the OSA for 1999, 2000 and 2001, and found questionable entries or omissions.¹⁷ In addition to questionable expenditure entries, the Year 2000 and 2001 Forms do not appear to accurately reflect the position held by the City's former Clerk/Treasurer.

The OSA compared the total City expenditures reported on the City's Financial Reporting Forms for 1999 through 2001 to the City's disbursements for 1999 and 2000, as reflected in cancelled City checks, and the total City expenditures reported in the Amended Year 2001 Form. It appears that the total City expenditures on the Year 1999 and 2000 Forms filed with the OSA by the City are substantially less than the disbursements made by the City during 1999 and 2000.

Auditor also had to obtain records from the City's bank to conduct the 2001 Audit. In order to dispose of government records, a city must adopt an approved records retention schedule, or prepare a schedule of the records to be disposed of for submission to the records disposition panel. Minn. Stat. § 138.17, subd. 7 (2002).

¹⁵ A city treasurer is required to deliver to a successor all books, papers and money belonging to the city. *See* Minn. Stat. § 412.141 (2002). The OSA understands that some City records in the former Clerk/Treasurer's possession or control were provided to the Lyon County Sheriff's Department after she was charged with theft. However, the OSA was informed that the records were poorly organized and did not appear to be complete. The OSA has not reviewed City records that are currently in the possession of the Lyon County Sheriff's Department.

¹⁶ A city clerk must keep a minute book. *See* Minn. Stat. § 412.151, subd. 1 (2002). Minutes must reflect the vote of each city council member on an action taken at a meeting, including, with certain exceptions, each member's vote on an appropriation of money. *See* Minn. Stat. § 13D.01, subd. 4 (a) and (b) (2002). Claims considered by a city council need not be given in full in the minute book if they are in other permanent records and can be identified from the minutes' description. *See* Minn. Stat. § 412.151, subd. 1 (2002). Additional items that must be reflected in the minutes include the city council members present, actions on motions, and the character of resolutions or ordinances. *See* Minn. Stat. §§ 13D.01; 412.151, subd. 1; and 412.191, subd. 3 (2002).

¹⁷ The City's reporting requirements are contained in Minn. Stat. § 471.698 (2002). The City filed Financial Reporting Forms in 1999, 2000 and 2001. The City also filed an Amended Financial Reporting Form in 2001, reflecting information obtained by the City's Auditor during the City's 2001 audit.

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The total City expenditures on the Year 2001 Form are far greater than the total City expenditures calculated by the City Auditor for the Amended Year 2001 Form.¹⁸

The Year 2000 and 2001 Forms report that the City has different individuals in the separate offices of clerk and treasurer. A city with combined offices of clerk and treasurer, and an annual revenue of \$100,000 or less, must have an audit at least once every five years.¹⁹ There is no audit requirement for cities with separate offices of clerk and treasurer. By reporting that the City had a separate clerk and treasurer, it appears the audit requirement could have been avoided.

The OSA recommends that the City work with its City Attorney and City Auditor to meet the City's obligations in managing the City's assets.²⁰ In addition, the OSA reminds the City that Financial Reporting Forms filed with the OSA must be accurate.

IV. Conclusion

A city council is responsible for establishing and maintaining internal controls. In fulfilling this responsibility, estimates and judgments are required to assess the expected benefits and related costs of internal control policies and procedures. The objective of internal controls is to provide the city council with reasonable, but not absolute, assurance that:

- Assets are safeguarded against loss from unauthorized use or disposition;
- Transactions are executed in accordance with the city council's authorization; and
- Transactions are recorded properly to permit the preparation of general purpose financial statements in accordance with generally accepted accounting principles.

We recognize that the City has a new Clerk/Treasurer, and has been working with the City Auditor. We understand that many of the weaknesses identified in this letter have already been corrected. We encourage the City to continue working with the City Attorney and the City

¹⁸ The comparisons are reflected below:

Year	Reported Total City Expenditures	Disbursements/ Amended Expenditures	Difference
1999	\$13,783.00	\$26,648.41	(\$12,865.41)
2000	\$16,791.00	\$27,021.33	(\$10,230.33)
2001	\$43,005.00	\$14,376.00	\$28,629.00

¹⁹ Minn. Stat. § 412.02, subd. 3 (2002). The audit must be for a one-year period to be determined at random by the person conducting the audit. *See also* Minn. Stat. § 412.591, subd. 2 (2002) (same for Optional Plan A cities with combined offices of clerk and treasurer). The City's annual revenues appear to be approximately \$21,000. *See also* Minn. Stat. § 412.151, subd. 2 (2002) (if the bookkeeping functions of the clerk are delegated to the city treasurer, an annual audit is required).

²⁰ The League of Minnesota Cities (LMC) has training programs for city officials, and maintains information for cities on their website: www.lmnc.org. For example, relevant research documents available on line from LMC include Procedures for Paying City Claims, Deposits and Investments, and Meetings of City Councils.

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Auditor on the issues raised in this letter. We remain available to provide any additional assistance you may need. If you have any questions regarding the findings and/or recommendations contained in this letter, please contact Ms. Nancy Bode at 651-297-5853.

Sincerely,

/s/ Carla Heyl

General Counsel/Deputy State Auditor

Enclosure

c: The Honorable Randy Stensgaard, Florence City Council Member
 The Honorable David Van Nevel, Florence City Council Member
 The Honorable Bruce Johnson, Florence City Council Member
 The Honorable Jeryld Hachmann, Florence City Council Member
 Ms. Dorothy Hachmann, Florence City Clerk
 Mr. David Meulebroeck, Florence City Auditor
 Mr. Glen A. Petersen, Florence City Attorney
 The Honorable Richard R. Maes, Lyon County Attorney