

Department of Legislative Services
Maryland General Assembly
2012 Session

FISCAL AND POLICY NOTE

House Bill 1328
Appropriations

(Delegate McDermott, *et al.*)

State Government - Independent Audits of Units - Requirement

This bill requires that beginning July 1, 2014, and every two fiscal years thereafter, each agency or unit of the Executive Branch of State government be audited by an independent auditor. Each audit must cover the immediately preceding two fiscal years. A report that contains the result of an audit must be submitted to the Department of Budget and Management (DBM) by December 31 of the fiscal year in which the audit was undertaken. DBM must contract with an independent auditor to complete the audits. The independent auditor may be paid only by receiving a percentage of any money recovered as a result of the audit.

Fiscal Summary

State Effect: General fund expenditures increase by \$76,100 in FY 2014 and by \$243,100 in FY 2017 for DBM to hire additional staff to coordinate and review the independent audits. Payments to independent auditors may total approximately \$10 million annually, with the cost paid through monies recovered as a result of the audits.

(in dollars)	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017
Revenues	\$0	\$0	\$0	\$0	\$0
GF Expenditure	0	76,100	226,300	232,200	243,100
Net Effect	\$0	(\$76,100)	(\$226,300)	(\$232,200)	(\$243,100)

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect

Local Effect: None.

Small Business Effect: Audit firms that perform the required audits may realize increased revenues. However, this will depend on the amount of monies recovered through the required audits.

Analysis

Current Law: Entities expending \$500,000 or more of federal grant funds are required, under the U.S. Office of Management and Budget (OMB) Circular A-133 Audit Compliance requirement, to obtain an audit (commonly referred to as the “Single Audit”) of those funds and the resulting grant funded programs by an outside independent audit firm.

At least once every three years, the Office of Legislative Audits (OLA) must conduct a fiscal/compliance audit of each unit of the State government, except for units in the Legislative Branch. Performance audits or financial statement audits must be conducted when authorized by the Legislative Auditor, when directed by the Joint Audit Committee or the Executive Director of the Department of Legislative Services (DLS), or when otherwise required by law. OLA has the authority to conduct a separate investigation of an act or allegation of fraud, waste, or abuse in the obligation, expenditure, receipt, or use of State resources. OLA may audit any county officer or unit that collects State taxes.

Within nine months of the issuance of an audit report, any agency with five or more repeat audit findings must report quarterly to OLA on (1) the corrective actions taken; or (2) a schedule for when corrective actions will be implemented. Subsequently, quarterly status reports must be submitted until satisfactory progress has been made to address the findings.

Background: The Single Audit is conducted on an annual basis in Maryland State Government for federal funded programs as required by OMB regulations. The audit considers waste, fraud, and abuse, and also reviews management practices, program results, and cash on hand. The intent is to ensure taxpayer dollars are being spent efficiently and effectively for their intended purpose.

OLA audits State agencies in the Executive and Judicial branches and other entities as requested by the Maryland General Assembly. OLA reports to the Joint Audit Committee and is responsible for:

- performing fiscal compliance audits of State agencies to evaluate fiscal operations and determine compliance with laws and regulations;
- conducting performance audits to evaluate whether a State agency or program is operating in an economic, efficient, and effective manner;
- conducting performance audits of the financial management practices of local school systems;
- operating a fraud hotline for reporting fraud, waste, and abuse of State resources;
- monitoring the financial reporting practices and financial condition of local governments in Maryland; and
- conducting special reviews and investigations.

When agencies submit required quarterly status reports, OLA subsequently reviews and responds to the agency via correspondence indicating which findings have been addressed as well as the findings for which continued reporting is necessary. Under this process, OLA does not perform any on-site work to verify an agency's representations of the actions taken.

OLA advises that 38 State agencies had three or more repeat findings in their last audit reports, totaling approximately 160 findings. The proposed fiscal 2013 State budget includes \$12.3 million in funding for the Office of Legislative Audits.

State Fiscal Effect: DBM must contract with one or more independent auditors to perform audits every two years for each unit of the Executive Branch. The cost for these independent audits could total approximately \$10 million a year, based on current expenditures at OLA. While the bill specifies that the independent auditor can only be paid through a portion of any monies recovered as a result of the audit, potential recoveries at many State agencies may be insufficient to cover the actual cost of conducting the independent audit. The potential for minimal cost recoveries is due to the nature of most State programs and ongoing internal efforts to realize recoveries. In addition, it is not certain if potential auditors will be found to provide services required by the bill for each Executive Branch agency and unit, given that payment will be contingent on money recovered from the audit.

In order to coordinate and review the independent audits, DBM will need to hire one procurement specialist at a cost of \$76,100 in fiscal 2014 and also two audit compliance analysts at a cost of \$226,300 in fiscal 2015 for the three positions. This estimate includes salaries, fringe benefits, one-time start-up costs, and ongoing operating expenses.

	<u>FY 2014</u>	<u>FY 2015</u>
Positions	1	3
Salaries and Fringe Benefits	\$71,056	\$215,699
One-time Equipment Purchases	4,485	8,970
Operating Expenses	<u>550</u>	<u>1,667</u>
Total State Expenditures	\$76,091	\$226,336

Future year expenditures could total \$243,122 by fiscal 2017 which reflect full salaries with annual increases and employee turnover as well as annual increases in ongoing operating expenses.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): State Department of Assessments and Taxation; Office of the Attorney General; Maryland Department of Agriculture; Department of Business and Economic Development; Board of Public Works; Department of Budget and Management; Department of Natural Resources; Maryland Department of Planning; Maryland State Department of Education; Maryland Department of the Environment; Governor's Office; Department of General Services; Department of Housing and Community Development; Department of Health and Mental Hygiene; Maryland Insurance Administration; Comptroller's Office; Department of Juvenile Services; Maryland State Lottery Agency; Department of Labor, Licensing, and Regulation; Maryland Energy Administration; Department of State Police; Morgan State University; Office of Administrative Hearings; Maryland Public Television; Maryland State Retirement Agency; College Savings Plans of Maryland; Department of Public Safety and Correctional Services; Maryland Stadium Authority; Maryland Department of Transportation; University System of Maryland; Department of Veterans Affairs; Department Legislative Services (Office of Legislative Audits); Department of Legislative Services

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