

LEGISLATIVE AUDIT DIVISION

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MEMORANDUM

TO: Members of the Legislative Audit Committee
FROM: Karen Cohlhepp, CPA, Financial-Compliance Audit Manager
Katie Majerus, CPA, Financial-Compliance Audit Supervisor
Steven Althoff, Senior Financial-Compliance Auditor
DATE: December 16, 2024
RE: Financial Audit Model Reform - Internal Service Fund and Charges for Services Fund Testing

Section 17-8-101(6), MCA, requires our office to audit and report on the reasonableness of internal service fund type fees and charges and on the fund equity balances as part of our regularly scheduled audits of state agencies. Section 17-2-302(3), MCA, requires our office to make a determination of whether money is or has been retained in a state charges for services fund contrary to the requirements of law as part of the financial audits we perform. Our team was tasked with determining whether the requirements in these laws continue to be relevant and necessary under the financial audit model envisioned under House Bill 132.

For fiscal years 2023 and 2024, we completed an analysis of internal service fund charges for services and fund equity balances for all funds. We have also completed the required analysis of charges for services state special revenue funds. Given we are no longer completing financial and compliance audits of every state agency, we plan to provide a stand-alone report for this work that we anticipate will be available in the March 2025 time frame.

For fiscal years 2025 and forward, we are in the process of determining whether there continues to be value in our office performing work over these funds, or if there are more prudent uses of our staff's time. We met with representatives from the Legislative Fiscal Division, Department of Administration, and Office of Budget and Program Planning to understand the other types of monitoring that occur over these funds and what level of reliance is placed on the work we currently perform. Based on our preliminary work, we believe there continues to be value in our office performing work over internal service funds. However, we do not believe there is enough risk in the state special revenue charges for services funds to continue requiring our office to perform specific work over these funds. We envision we will pursue a statutory change in the 2027 Legislative Session to remove the requirement for our office in §17-2-302(3), MCA.

For internal service funds, there have been substantial changes in the governmental accounting standards since the requirement in §17-8-101(6) became effective. These changes in standards complicate the analysis of the reasonableness of fund balance and introduce subjectivity to our work and the analysis. While we continue to see value in our office performing work over internal service funds given their role in state government, we are interested in whether our

current work provides that value, or if other information and analysis would be helpful. Our next steps are to work with legislators, including the Legislative Audit Committee, to better understand how we can bring value to them through our work. In particular, we will be soliciting feedback on the following:

- Whether our current work over the funds is useful in their work as appropriators.
- What information do they rely on from the agencies, that might be helpful to have assurance over.
- What measurements are useful (Working Capital, Fund Balance, etc.)
- Whether it's more useful to see the underlying financial schedule data or to see our conclusion about it.
- The level of detail desired in the report and whether it is useful in include information available elsewhere.
- What situations have caused legislator interest in internal service funds in the past to determine whether we can present similar information in a systematic manner for all internal service funds.

We intend to solicit this feedback after publishing the report for fiscal years 2023 and 2024, to allow legislators time with the new report and its content.