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FISCAL IMPACT REPORT

SPONSOR Candelaria **ORIGINAL DATE** 01/27/14
LAST UPDATED _____ **HB** _____
SHORT TITLE State Inspectors General Act **SB** 13
ANALYST Cerny

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

| | FY14 | FY15 | FY16 | 3 Year Total Cost | Recurring or Nonrecurring | Fund Affected |
|--------------|------|---------------|---------------|----------------------|------------------------------|------------------|
| Total | | Indeterminate | Indeterminate | Indeterminate | Recurring | General Fund |

(Parenthesis () Indicate Expenditure Decreases)

Companion to SJR 1

SOURCES OF INFORMATION

LFC Files

Responses Received From

Office of the Attorney General (AGO)
 Children, Youth and Families Department (CYFD)
 Department of Transportation (DOT)
 Public Education Department (PED)
 Office of the State Auditor (OSA)
 New Mexico Corrections Department (NMCD)
 New Mexico Higher Education Department (NMHED)

SUMMARY

Synopsis of Bill

Senate Bill 13 would create Offices of Inspectors General (OIG) for nine cabinet departments. The OIG would be appointed by the state auditor based upon relevant abilities as listed in the act and without regard to political affiliation. The OIG are to report directly to the State Auditor. Each OIG office would be operationally separate from other divisions of its department.

The nine affected departments are Children, Youth and Families, Corrections, Health, Higher Education, Human Services, Public Education, Finance and Administration, Transportation, and Taxation and Revenue.

SB 13 establishes the authority of each office of the OIG to:

- conduct internal and compliance audits and investigate its department and related state-funded entities for efficiency, proper use of public funds, and to prevent fraud, waste and abuse;
- unrestricted access to records, data, reports, contracts, memoranda, correspondence and any other information necessary to carry out the duties of its office;
- coordinate with state auditor, the legislature, and the Medicaid fraud and elder abuse divisions of the Attorney General’s Office;
- recommend changes and provide progress reports on improvements;
- refer potential criminal matters to the state auditor, the attorney general, or to a district attorney;
- gather, analyze, and validate department and state-funded entity information as requested by the governor or interim legislative committee;
- validate performance measures and provide post financial audit progress reports;
- contract for professional services;
- accept federal funds for performance of its duties;
- adopt professional standards.

Further, SB 13 requires each OIG to abide by the following reporting requirements: an annual work plan is to be submitted to the state auditor and to an interim legislative committee appointed by the legislative council; results of audits and investigations, to be submitted to the state auditor, the interim legislative committee, and the public; an annual report is to be issued by September 1 detailing findings and cost savings, recommendations made to its department and related state-funded entities, and progress on the resolution of findings, saved or recovered public money, and implementation of recommendations.

The bill restricts the OIG from performing audits of departments’ financial statements or publicly disclosing information or records made confidential by law or exempt from the Inspection of Public Records Act.

SB13 also provides definitions for the terms “department” and “state-funded entity.”

FISCAL IMPLICATIONS

It is assumed the SB 13 anticipates utilization of existing staff to carry out its purposes as it carries no appropriation of funds. Most of the departments named in this bill already have established Inspector General Offices, internal audit or compliance units. In CYFD, for example, the Inspector General already performs the duties listed in the bill, and has the authority granted in the bill. NMDOT has its own OIG, which has twenty-one staff employees, including the investigations and audits sections. NMDOT’s OIG budget is approximately \$1.5 million for salaries, benefits and other expenditures required to run the office.

SB 13 provides that the “the state auditor shall establish and maintain offices of inspectors generals” in the departments listed but it does not provide an appropriation to the OSA to carry out this function. OSA analysis states that the bill does not “provide an appropriation to support personnel, furniture, equipment and other resources necessary to establish offices of inspector general in the departments listed. The fiscal impact of this bill could be significant, but without further study and clarification of the bill’s language it is difficult to estimate the exact fiscal

impact. It is important to note that the current operational budgetary resources of the OSA would not be sufficient to carry out the purposes of this legislation.” Further, OSA analysis states that “it is likely that significant recurring funding will be required to implement the provisions of this bill.”

NMCD analysis cites a concern with duplication of resources and functions.

SIGNIFICANT ISSUES

The State Inspectors General Act in SB 13 seeks to improve the executive branch’s effectiveness to evaluate their programs and to investigate potential waste, fraud and abuse within state agencies and other entities. Though not in statute, many executive cabinet departments carry out various government accountability functions, including internal and compliance audits and investigations, through inspector general, internal audit and quality assurance offices. However, these government accountability functions often are not independent, have misdirected or insufficient effort and their work is often not coordinated or reported to the Legislature, according to past LFC staff analysis. SB 13 would create a consistent set of responsibilities for these internal auditing units including collaboration with the state accountability function. This coordination is important to maximize the use of the state’s accountability functions including the Legislative Finance Committee, which performs in-depth program evaluations, Office of State Auditor, which performs financial statement audits, and the Office of Attorney General, which performs civil/criminal investigations and prosecution, including for Medicaid.

However, the proposed reporting structure may make it difficult for the executive agencies to identify and address in a timely manner matters for which they are ultimately responsible. The State Auditor is an elected official who has the power, duty and authority to examine and pass upon activities of state officers and agencies. It is the executive’s role and responsibility to meet statutory obligations and to execute the laws passed by the Legislature. Although the proposed offices would be attached to and would address matters relating to executive agencies, neither the governor nor cabinet secretaries are included in the bill as persons to whom reports on the results of audits and investigations would be provided or of the annual work plans to be submitted by the offices.

The OSA in its analysis raises as significant issues conflicts with requirements of professional standards such as the Generally Accepted Government Auditing Standards (GAGAS) and the Public Accountancy Act with regard to the independence of both internal and external auditors that would arise from the reporting structure.

Specifically, OSA analysis states:

“State law and professional auditing and accounting standards require the State Auditor to function as an external auditor. Generally Accepted Government Auditing Standards (GAGAS), to which the State Auditor is required to adhere as an external auditor in the performance of financial audits and other attestation engagements, require that the State Auditor and his independent auditors be free from impairments to independence and avoid the appearance of such impairments.” According to OSA analysis, “the bill’s provisions would result in the impairment of the State Auditor’s organizational independence to conduct the annual financial audits of the departments because the external audit function (the

State Auditor) would be organizationally located within the reporting line of the areas under audit (the departments).”

“The bill’s requirement that the State Auditor ‘maintain’ the offices and that the offices report directly to the State Auditor also cause organizational independence problems for the internal audit function of the inspectors general. By definition, internal auditors work for the management of the audited entities, not the management of entities external to the organization. In accordance with the Institute of Internal Auditors’ Standards for the Professional Practice of Internal Auditing (which internal auditors are required to use in conjunction with GAGAS), it is vital that offices of inspector general be free from organizational impairments to their independence. Additionally, the bill requires offices of inspectors general to report results of audits, including internal audits, to the ‘state auditor, the appropriate interim legislative committee appointed by the New Mexico legislative council and the public.’ The bill notably omits a requirement that the offices of inspectors general report the results directly to those charged with governance of their respective departments. By not requiring the offices of inspector general to report to those charged with governance (department heads), the bill’s provisions run contrary to the independence requirements of GAGAS.”

NMCD’s analysis specifically addresses personnel issues related to the reporting structure, stating that the bill “does not clearly indicate who employs, supervises and terminates or disciplines the inspectors general and any staff hired or used by them. Having the inspectors general report both to the agency secretary (if the inspector general and related staff are NMCD employees) and to the State Auditor may cause competing interests and inefficiency. For example, who can discipline the inspector general and associated staff for misconduct—the agency (NMCD) or the State Auditor? Who gets to make the hiring decisions for the staff used to aid the inspector general in the performance of his duties—the agency or the State Auditor? Are the inspector general and his staff State Auditor employees merely employees of the State Auditor administratively assigned to an agency, or are they that agency’s employees? If they are to be agency employees, does not the relevant agency needs to be able to hire, train and discipline them? If they are to be State Auditor employees, the State Auditor needs to assume the responsibility and costs for hiring, training and disciplining the employees.”

The bill clearly states that the OIGs may not publicly disclose information or records made confidential by law or exempt from the Inspection of Public Records Act. Nonetheless, analysis from the AG and PED expressed concern about confidentiality requirements since Section 4(B)(2) of the bill would give each office of the OIG “unrestricted access to records, data, reports, contracts, memoranda, correspondence and any other information necessary to carry out the duties of the office.”

Analysis of the AGO notes that the bill grants authority to OIGs outside their department’s jurisdiction.

PED analysis states “Federal law prohibits sharing student information with other agencies without demonstration of an educational purpose. (See the Family Educational Rights and Privacy Act, FERPA, at 20 U.S.C. § 1232g; 34 CFR Part 99). Thus, the state law would violate the federal act.” However OIG functions outlined in the bill appear to fall within allowable use of this information for audit and accountability work.

PERFORMANCE IMPLICATIONS

As noted earlier, NMDOT currently has its own OIG. NMDOT analysis states, “If this office is moved to the State Auditor, the effectiveness of the OIG may be compromised in cases where an immediate response is needed in urgent situations.”

CYFD analysis states “the bill's requirement for IGs to develop work plans and submit reports to both the SAO and an interim legislative committee, and to coordinate their activities with the SAO and the Medicaid Fraud and Elder Abuse Division of the Attorney General's Office, will likely prove to be cumbersome and will certainly take time away from internal audits and reviews and other investigations requested by the CYFD secretary.”

The AGO and several district attorneys' offices may see a slight increase in the number of cases referred to them for prosecution.

ADMINISTRATIVE IMPLICATIONS

NMDOT analysis states “The bill does not specify how the offices will be funded, or to what agency or office the employees of those offices are attached for purposes of personnel budget and management. However, if it is intended that those personnel are to be paid and managed by the State Auditor, NMDOT's OIG currently has 21 full-time employees that would require transfer to the personnel management system of the State Auditor.”

COMPANIONSHIP

SB 13 is related to SJR 1 which proposes a constitutional amendment that would require the creation of OIG in designated state agencies, appointed and managed by the State Auditor.

AMENDMENTS

Analysis from the AGO suggests that an amendment to Section 4(B)(2) to limit authority of the OIG to obtain information should be considered.

CAC/jl