

NORTH DAKOTA LEGISLATIVE COUNCIL

Minutes of the

LEGISLATIVE AUDIT AND FISCAL REVIEW COMMITTEE

Tuesday, August 10, 2004
Roughrider Room, State Capitol
Bismarck, North Dakota

Senator Randel Christmann, Vice Chairman, called the meeting to order at 9:00 a.m.

Members present: Representatives Larry Bellew, Jeff Delzer, Andrew Maragos, Bob Skarphol, Blair Thoreson, Mike Timm, Lonny Winrich; Senators John M. Andrist, Randel Christmann, Jerry Klein, Aaron Krauter

Members absent: Representatives Ole Aarsvold, Al Carlson, RaeAnn G. Kelsch, Francis J. Wald, Amy Warnke

Others present: See attached Appendix A

It was moved by Representative Skarphol, seconded by Senator Klein, and carried on a voice vote that the minutes of the April 19, 2004, meeting of the Legislative Audit and Fiscal Review Committee be approved as distributed.

ADJUSTMENTS AND CORRECTIONS OF TAX DISTRIBUTION PAYMENTS TO POLITICAL SUBDIVISIONS

Vice Chairman Christmann called on Mr. John Bjornson, Legislative Council attorney, who presented a bill draft [50099.0100] providing for statutory authority for the State Treasurer to make adjustments to ensure proper distributions to the political subdivisions. The committee later in the meeting decided not to make any recommendations regarding the bill draft.

Vice Chairman Christmann called on Mr. Paul Welk, State Auditor's office, who presented information relating to the office's review of the State Treasurer's office accuracy of tax distribution recalculations and the plan for correction or adjustment of payments to affected cities, counties, and school districts. A copy of the information presented is on file in the Legislative Council office. Mr. Welk said the recalculations were conducted for the time periods cited to be in error in the audit for the following distributions:

- State highway tax (December 2000 - December 2002).
- State aid (September 2001 - December 2003).
- Coal severance tax (August 2001 - February 2004).
- Coal conversion tax (November 2002 - November 2003).
- Oil and gas production tax (July 2000 - June 2004).

Mr. Welk said the State Auditor's office prepared spreadsheets for each type of tax distribution to verify the State Treasurer's office recalculations. He said the review of the State Treasurer's office recalculations identified numerous errors. He reviewed the types of errors noted and provided the list of tax distribution overpayments and underpayments to cities, counties, and school districts as calculated by the State Auditor's office. He said based on the errors noted in the review and the lack of internal controls surrounding the distributions administered by the State Treasurer's office, the State Auditor's office can make no assurance that future distributions will be accurate.

In response to a question from Senator Christmann, Mr. Welk said some of the types of errors identified in the original audit findings were not corrected in the recalculations.

In response to a question from Representative Maragos, Mr. Welk said it took the auditor conducting the review approximately 152 hours to develop the distribution spreadsheets, compare the totals to the State Treasurer's office recalculations, and resolve the discrepancies. He said this does not include time incurred by supervisors or managers.

In response to a question from Senator Krauter, Mr. Welk said the specific recalculation errors for cities, counties, and school districts are detailed in the workpapers. He said because the workpapers include several hundred pages of documentation, they were not provided to the committee. Senator Krauter said it is "unfair" to comment on errors discovered and not to provide the supporting documentation for the comments. He said the recalculation schedules provided by the State Treasurer's office were identified as a draft.

In response to a question from Senator Christmann, Mr. Welk said the redistribution payments to each city, county, and school district will be issued or collected on a net basis, rather than by specific type of distribution. He said as each overpayment is refunded or corrected, the corresponding funds will be redirected to political subdivisions that were underpaid.

In response to a question from Representative Skarphol, Mr. Welk said the State Auditor's office believes the inability to accurately calculate

distributions is due to a lack of qualified personnel and proper internal controls in the State Treasurer's office.

In response to a question from Representative Winrich, Mr. Welk said the most recent audit of the State Treasurer's office did include a finding related to the qualification of the controller position. He said the report did not include internal control recommendations. He said the State Auditor's office is willing to work with the State Treasurer's office to improve its internal controls.

In response to a question from Representative Skarphol, Mr. Welk said many of the errors discovered were specific to the audit period, such as the use of updated population amounts and implementing changes in legislation. He said there are some cases where the errors may have resulted from differences in interpretation of law. He said in those cases the State Auditor's office consulted with the Attorney General's office to determine the correct procedure.

In response to a question from Representative Timm, Mr. Welk said he believes the next State Treasurer elected would have the authority to correct any distribution errors made by the current State Treasurer.

In response to a question from Senator Krauter, Mr. Welk said the most recent audit included a recommendation that the State Treasurer's office either periodically contact or make arrangements to receive notification from the Secretary of State's office regarding dissolution of cities.

Ms. Kathi Gilmore, State Treasurer, said 83 percent of the incorrect payments to political subdivisions have been corrected. She said 94 percent of the payments will be corrected by October 2004. She said the State Treasurer's office will work with the political subdivisions to develop extended repayment schedules if necessary. She said the North Dakota Association of Counties and North Dakota League of Cities were notified of and agree to the correction process.

Ms. Gilmore said the State Treasurer's office method of calculating distributions has not changed from previous years, yet the State Auditor's office did not make any related recommendations or findings in previous audits. She said the State Auditor's office should have identified these findings years ago.

In response to a question from Senator Christmann, Ms. Gilmore said she has talked to the superintendent of the Center School District. She said the superintendent was concerned but "understanding" regarding the repayment process.

In response to a question from Representative Maragos, Ms. Gilmore said the person currently employed as the controller in the State Treasurer's office does not have an accounting degree. She said she has employed certified public accountants in the controller position in the past who were not as good as the current controller.

In response to a question from Representative Skarphol, Ms. Gilmore said she believes the State Auditor's office has "gone back far enough" in its review of distributions. She said the State Auditor's office can decide if it wants to review previous distributions.

In response to a question from Representative Timm, Ms. Gilmore said it is the duty of the State Auditor's office to find mistakes. She said agencies should work together to expedite corrections.

In response to a question from Senator Christmann, Ms. Gilmore said the delay in the correction process was due to the time necessary for the auditor to build spreadsheets, during which time the auditor also worked on other audits.

In response to a question from Senator Christmann, Ms. Kathy Kirschman, Deputy State Treasurer, State Treasurer's office, said the recalculations were done by an individual in the State Treasurer's office other than the individual in the office who made the original calculations. She said this was done to follow the State Auditor's recommendation that additional staff provide "backup" for determining and verifying the distributions. She said mistakes were also made by the State Auditor's office in calculating the distributions. She said these errors were discovered by the State Treasurer's office.

In response to a question from Senator Christmann, Ms. Kirschman said she does not believe there will be future errors in distributions. She said spreadsheets are now available which will provide support for the totals generated from the mainframe computer.

In response to a question from Senator Christmann, Ms. Gilmore said there have been no "major dissenters" to the distribution correction plan. Senator Christmann said there are "major dissenters" in Oliver County. He said some political subdivisions cannot generate the revenues necessary to repay distributions due to mill caps. He said the Center School District is a small district, which will have to eliminate programs to adjust for the differences in payments.

In response to a question from Senator Christmann, Ms. Gilmore said the State Treasurer's office has been understaffed and underfunded for a number of years. She said she has confidence in the abilities of her staff.

In response to a question from Senator Christmann, Ms. Gilmore said the State Treasurer's office has not yet prepared any legislation to address ambiguities in the North Dakota Century Code relating to the State Treasurer's office referred to in the audit.

In response to a question from Representative Winrich, Ms. Kirschman said the State Treasurer's office used the 1990 census figures in calculating state aid distributions in April 2003 because the office was not aware the 2000 census data was made available in March 2003. She said historically the new

census data had not been released until July. She said for the July 2003 distribution, the State Data Center provided estimated rather than actual census data for state aid distribution calculations, which were used incorrectly.

In response to a question from Representative Delzer, Ms. Kirschman said the Attorney General's office directed the State Treasurer's office to redistribute the payments in the simplest way possible.

In response to a question from Senator Christmann, Ms. Gilmore said payment forms sent to political subdivisions include a summary of adjustments made due to previous miscalculations and the corresponding funds affected by the adjustments.

In response to a question from Representative Delzer, Mr. Edward Erickson, Assistant Attorney General, Attorney General's office, said the political subdivisions will be able to correct the balances in each of the funds as long as they know where to direct the corrected payments. He said there are no funds missing, they are only misdirected to the wrong political subdivision.

In response to a question from Representative Maragos, Mr. Erickson said the tax distribution payments can vary significantly from one period to the next. He said political subdivisions primarily rely on the State Treasurer's office and the State Auditor's office to assure the payments received are correct.

In response to a question from Representative Skarphol, Mr. Erickson said based on controlling law, political subdivisions are not entitled to retain the overpayments. He said there is no legal impediment to the reallocation process.

Mr. Welk said he is not certain how the State Treasurer's office determined that distribution calculation errors were made by the State Auditor's office. He said the State Auditor's office spreadsheets and calculations were not made available to the State Treasurer's office in order to maintain auditor independence.

In response to a question from Representative Maragos, Mr. Welk said it is not feasible for political subdivisions to recalculate their own tax distribution payments. He said the State Treasurer's office needs to formulate a plan to assure distributions are correct.

In response to a question from Representative Delzer, Ms. Kirschman said the spreadsheets used by the State Treasurer's office are not "write-protected." She said any necessary formula maintenance will be required to be reviewed by a second individual.

Representative Delzer asked that the State Treasurer's office repayment schedule be mailed to members of the Legislative Audit and Fiscal Review Committee. A copy of the information is on file in the Legislative Council office.

Mr. Welk presented information on a review conducted of the Tax Commissioner's office cigarette tax distribution recalculations and the plan for correction or adjustment of payments to affected cities. A

copy of the information presented is on file in the Legislative Council office. He said the Tax Commissioner's office audit report for the biennium ended June 30, 2003, identified that \$6,738 was incorrectly deposited into the general fund that should have been deposited into the cigarette tax distribution fund. He said the State Tax Commissioner's office corrected the error in November 2003 by depositing \$6,738 of general fund receipts into the cigarette tax distribution fund, which was then distributed to the affected cities during that same month.

In response to a question from Representative Delzer, Mr. Welk said it took only a few minutes to verify that the error was properly corrected.

In response to a question from Representative Maragos, Mr. Welk said the State Treasurer's office is responsible for making distributions to cities from the cigarette tax distribution fund. He said the State Treasurer's office does not have the ability to verify the accuracy of the Tax Commissioner's office collections and deposits.

Mr. Welk presented information regarding state agencies that either collect or distribute taxes and whether the agency employs an individual with an accounting degree. A copy of the information presented is on file in the Legislative Council office. Mr. Welk said the agencies that collect or distribute taxes are:

- State Treasurer's office.
- Tax Commissioner's office.
- Attorney General's office.
- Insurance Department.
- Department of Transportation.
- Highway Patrol.
- Aeronautics Commission.

Mr. Welk said all of the agencies listed employ an individual with an accounting degree with the exception of the State Treasurer's office and the Aeronautics Commission.

In response to a question from Representative Maragos, Mr. Welk said during the most recent audit periods prior to the 2001-03 biennium, the State Treasurer's office has employed at least one individual with an accounting degree.

In response to a question from Senator Christmann, Mr. Welk said the Aeronautics Commission is responsible for collecting aviation fuels taxes. He said the taxes are deposited into a fund for grants to airports.

In response to a question from Representative Delzer, Mr. Welk said the State Treasurer's office is responsible for most of the state's tax distributions. He said other state entities that distribute taxes generally have established procedures for an internal review of the calculations.

PERFORMANCE AUDITS

Vice Chairman Christmann called on Mr. Gordy Smith, State Auditor's office, who presented the

performance audit report of the Administrative Committee on Veterans Affairs and the Department of Veterans Affairs as of March 22, 2004. Mr. Smith said North Dakota Century Code (NDCC) Section 54-10-01 requires the State Auditor's office to conduct performance audits in accordance with generally accepted government auditing standards. He discussed the following primary goals of the performance audit and the related recommendations and findings:

1. Is management and the organizational structure of the Department of Veterans Affairs effective?
 - a. Request the Attorney General's office review commissioner's actions.
 - b. Make improvements to the Administrative Committee on Veterans Affairs.
 - c. Add a conservatorship program.
 - d. Review a position's duties and responsibilities in relation to processing federal claims at the federal Department of Veterans Affairs regional office in Fargo.
 - e. Improve employee supervision.
 - f. Make improvements relating to county veterans' service officers.
 - g. Develop strategic plans.
 - h. Improve dissemination of information.
2. Is the Administrative Committee on Veterans Affairs and the Department of Veterans Affairs using financial resources efficiently and effectively?
 - a. Obtain proper appropriation authority.
 - b. Make improvements to the loan program.
 - c. Make improvements to the grant program.

Attached as Appendix B is the listing of the recommendations included in the performance audit.

In response to a question from Representative Maragos, Mr. Smith said two employees of the Department of Veterans Affairs were identified as conservators for veterans, one of which was the commissioner. He said the commissioner's responses to questions regarding his conservatorship responsibilities and duties were contradicted by other information obtained. He said the State Auditor's office has asked the Attorney General to consider whether the commissioner of the Department of Veterans Affairs was in noncompliance with NDCC Section 54-10-23 by obstructing or misleading the State Auditor's office or by hindering a thorough examination. In addition, the Attorney General was asked to consider determining whether department employees performed conservator duties on state time using state resources. He said he is uncertain what actions the Attorney General will take regarding the requests. He said the previous commissioner retired in May 2004.

In response to a question from Representative Maragos, Mr. Smith said the State Auditor's office

recommends the Administrative Committee on Veterans Affairs take appropriate action to modify NDCC Section 37-18.1-01 to reduce its current membership of 15 to a more manageable size of approximately seven members. He said the committee's membership consists of three members from each of the five major veterans' organizations in the state. He said the State Auditor's office recommends the committee appointment process be modified to more accurately reflect the membership size of each of the veterans' organizations. He said the State Auditor's office is not aware of opposition from veterans' organizations regarding the recommendation to change committee membership.

Vice Chairman Christmann called on Mr. Rudy Jenson, Interim Chairman, Administrative Committee on Veterans Affairs. He said the committee is committed to addressing the findings included in the performance audit report for both the Administrative Committee on Veterans Affairs and the Department of Veterans Affairs. He said a new commissioner will be hired for the Department of Veterans Affairs by the end of August 2004.

In response to a question from Representative Maragos, Mr. Jenson said the Administrative Committee on Veterans Affairs has not yet made a decision regarding changing the committee membership size.

In response to a question from Representative Maragos, Mr. Eric Monson, Managing Partner, Novus, LLC, said Novus was hired to do the strategic plan for both the Veterans Home and the Department of Veterans Affairs. He said the makeup of the administrative committee will be studied during the preparation of the department's strategic plan.

In response to a question from Senator Christmann, Mr. Monson said the strategic planning committee for the Department of Veterans Affairs held its first meeting in July 2004 and the strategic plan should be completed by the middle of October 2004. Mr. Jenson said the meetings are open to the public and the meeting dates are available through the Secretary of State's office.

In response to a question from Representative Skarphol, Mr. Monson said the strategic plan will include a detailed operating plan addressing all areas of the department's operations.

Mr. Smith said the Administrative Committee on Veterans Affairs has continuing appropriation authority for the interest income of the veterans' postwar trust fund but this continuing appropriation does not extend to the Department of Veterans Affairs.

Mr. Smith said in the 2001-03 biennium, veterans' postwar trust fund money was used for department expenses, including grants, employee salaries and benefits, and operations. He said appropriation authority was not obtained by the department for these expenditures.

In response to a question from Representative Skarphol, Mr. Smith said according to the Office of Management and Budget, the department's salaries, benefits, and other operating expenditures are paid from veterans' postwar trust fund money by the Administrative Committee on Veterans Affairs. He said, however, the Attorney General's office agreed with the State Auditor's office that the department is receiving and expending money from the veterans' postwar trust fund.

In response to a question from Representative Delzer, the legislative budget analyst and auditor said one should be able to determine whether the Administrative Committee on Veterans Affairs granted money from the veterans' postwar trust fund to the Department of Veterans Affairs or directly paid the expenses from the fund. Ms. Sheila Peterson, Director, Fiscal Management Division, Office of Management and Budget, said there is a separate account maintained at the Bank of North Dakota for the veterans' postwar trust fund. She said the payment of specific expenses are made from the veterans' postwar trust fund account and there is no intermingling of funds.

In response to a question from Representative Delzer, Ms. Peterson said the percentage of salaries paid from the veterans' postwar trust fund did not change from what was approved by the Legislative Assembly.

Representative Skarphol said the proceeds from the veterans' postwar trust fund should be spent on veterans' programs, not on staff salaries.

In response to a question from Senator Andrist, the Legislative Council staff distributed a copy of an analysis of the veterans' postwar trust fund. A copy of the information provided is available in the Legislative Council office. The legislative budget analyst and auditor said 1996 initiated constitutional measure No. 4 provided for the veterans' postwar trust fund to be a permanent trust fund and for all income received from the fund's investments to be appropriated on a continuing basis to the Administrative Committee on Veterans Affairs for programs which are of benefit and service to veterans or their dependents.

Mr. Smith said the Department of Veterans Affairs has six employees; however, because two employees have one-half of their salaries paid for from the veterans' postwar trust fund, only five full-time equivalent (FTE) positions are identified in the department's budget. Representative Delzer said the House Human Resources Committee was aware of the "off-budget" FTE; however, the committee felt it could not control spending from the veterans' postwar trust fund.

In response to a question from Representative Delzer, the legislative budget analyst and auditor said 2003 Senate Bill No. 2015 directs state agencies and institutions to report on their continuing appropriations as part of their budget presentation to the

Appropriations Committees of the Fifty-Ninth Legislative Assembly. He said the report is to include justification for continuing the authority, expenditures made pursuant to the continuing appropriation and related revenues and fund balances for the 1999-2001 biennium, the 2001-03 biennium, the 2003-05 biennium to date, and projections for the 2005-07 biennium.

Representative Skarphol said a Legislative Council staff analysis of vacant FTE and off-budget FTE positions will be presented to the Budget Section during its October 2004 meeting.

In response to a question from Representative Delzer, the legislative budget analyst and auditor said many of the off-budget FTE positions are pursuant to authority provided by the Legislative Assembly, including positions funded with higher education tuition revenues and agriculture commodity groups being granted continuing appropriation authority.

In response to a question from Representative Delzer, Mr. Smith said the Veterans Home performance audit followup report will be available during the 2005 Legislative Assembly.

Representative Delzer said the Administrative Committee on Veterans Affairs will be asked to provide information to the Fifty-Ninth Legislative Assembly regarding progress in addressing the audit findings. Mr. Smith said 2003 House Bill No. 1007 directs the State Auditor's office to file the results of the performance audit with the Appropriations Committees during the 2005 Legislative Assembly.

It was moved by Representative Maragos, seconded by Senator Krauter, and carried on a roll call vote that, pursuant to NDCC Section 54-35-02.2, the committee accept the performance audit report of the Administrative Committee on Veterans Affairs and Department of Veterans Affairs as of March 22, 2004. Representatives Bellew, Delzer, Maragos, Skarphol, Thoreson, Timm, and Winrich and Senators Andrist, Christmann, and Krauter voted "aye." No negative votes were cast.

REQUEST FOR PERFORMANCE AUDIT CONSULTANT

Mr. Smith presented information to the committee regarding bids from consultants for the Department of Corrections and Rehabilitation performance audit pursuant to NDCC Section 54-10-01. He said during the December 22, 2003, meeting of the Legislative Audit and Fiscal Review Committee, a motion was approved for the State Auditor's office to hire a consultant to assist with conducting the Department of Corrections and Rehabilitation performance audit at a cost not to exceed \$50,000 and that any consultant costs in excess of \$50,000 are subject to prior approval by the Legislative Audit and Fiscal Review Committee.

Mr. Smith said a request for proposal was sent to 13 entities, of which seven were returned to the State

Auditor's office. He said the request for proposal provided for the following study areas:

- Evaluate treatment programs.
- Medical program and contracted medical services.
- Options for prison overcrowding, including cost estimates, benefits, and challenges associated with each option.
- Management and administration structure of the Department of Corrections and Rehabilitation.

Mr. Smith said the cost of the proposals returned ranged from \$50,000 to \$109,000. He said based on evaluations of each of the entities, Criminal Justice Institute, Inc., which submitted a bid of \$52,475, was chosen as the consultant. As a result, he said, he is requesting approval by the committee to spend a total of \$52,475 for the consultant. He said the Department of Corrections and Rehabilitation provided recommendations relating to the request for proposal and reviewed each of the seven bids that were received. He said the State Auditor's office made the final decision on the consultant. He said pursuant to NDCC Section 54-10-01, the agency that is audited is required to pay the cost of the consultant.

In response to a question from Senator Krauter, Mr. Dave Krabbenhoft, Fiscal Director, Department of Corrections and Rehabilitation, said the department has conducted some studies that are addressed in the request for proposal but not to the extent of what will be done by the consultant. He said the department welcomes assistance that may be provided by the performance audit. He said he is not aware of any federal grants available to pay for the cost of the consultant.

It was moved by Representative Delzer, seconded by Representative Skarphol, and carried on a roll call vote that, pursuant to NDCC Section 54-10-01, the committee approve the State Auditor's office request to hire Criminal Justice Institute, Inc., at a total cost of \$52,475--or an additional \$2,475 more than previously approved--as a consultant to assist with conducting the Department of Corrections and Rehabilitation performance audit. Representatives Bellew, Delzer, Skarphol, Thoreson, Timm, and Winrich and Senators Andrist, Christmann, Klein, and Krauter voted "aye." No negative votes were cast.

AUDIT GUIDELINES FOR STATE AGENCIES - 12 QUESTIONS

The Legislative Council staff reviewed a memorandum entitled *Audit Report Presentation Guidelines*. The Legislative Council staff said the memorandum provides information on the history of the 12 questions required to be addressed by auditors of state agencies, boards, and institutions as well as the suggested list of six questions to replace the 12 questions as proposed by the State Auditor's office. The

Legislative Council staff said the memorandum also includes eight suggested areas that auditors could review with the Legislative Audit and Fiscal Review Committee.

Senator Christmann said there is no urgency for the committee to take action on changing the 12 questions. He said he would prefer the committee address the 12 questions at a time when Chairman Wald is present.

Mr. Nagel presented information on suggested changes to the 12 questions. A copy of the information presented is on file in the Legislative Council office. Mr. Nagel said the State Auditor's office believes auditor communication with the Legislative Audit and Fiscal Review Committee can be improved by restructuring the 12 questions to the following six:

1. What type of report has the auditor issued on the financial statements of the agency?
2. Was there compliance with statutes, laws, rules, and regulations under which the agency was created and is functioning?
3. Was internal control adequate and functioning effectively?
4. Were there any indications of lack of efficiency in financial operations and management of the agency?
5. Has action been taken on findings and recommendations included in prior audit reports?
6. Was a management letter issued? If so, provide a summary below, including any recommendations.

Mr. Nagel said additional communications can be provided to the committee regarding significant accounting policies, management judgments and accounting estimates, audit adjustments, disagreements with management, consultation with other independent auditors, major issues discussed with management prior to retention, and difficulties encountered in performing the audit.

In response to a question from Representative Skarphol, Mr. Nagel said Legislative Audit and Fiscal Review Committee members could be notified when state entities, who use the services of an independent auditor, have their meeting with private auditors to review their audit report.

Senator Christmann said current question No. 7 (was there any indication of fraud or dishonesty?) and No. 12 (has the agency developed budgets of actual anticipated expenditures and revenues on at least a quarterly basis, and compared, on at least a quarterly basis, actual expenditures and revenues on the accrual basis to budgeted expenditures and revenues?) are questions that should be kept.

Senator Krauter said the proposed six questions do not fully address issues relating to appropriations that are addressed in current question No. 10 (were all activities of the agency encompassed within appropriations of specific amounts?) and question No. 12.

The legislative budget analyst and auditor said representatives of Brady, Martz & Associates, P.C., and Eide Bailly LLP have previously agreed with the State Auditor's office proposal to change the 12 questions. He said the Government Performance and Accountability Committee is considering a bill draft which would direct the State Auditor's office to address performance measures when conducting audits of state agencies and institutions. He said if the bill draft is approved, the Legislative Audit and Fiscal Review Committee may want to adjust the questions to reflect findings related to performance measures.

The committee recessed for lunch from 11:50 a.m. to 1:00 p.m.

BOARD OF MESSAGE AUDIT REPORT

Vice Chairman Christmann reviewed a letter received from Mr. Thomas L. Elliott, Certified Public Accountant, West Fargo, who audited the Board of Message audit for the years ended June 30, 2003 and 2002. He said the letter indicates that the audit report contained an unqualified opinion and did not include any findings or recommendations. A copy of the letter is on file in the Legislative Council office.

Mr. Erickson said the former secretary-treasurer was found to have improperly used Board of Message funds. He said a settlement was reached and approximately \$6,000 was repaid to the board. He said the individual is no longer on the board. He said the state's attorney decided there was no merit to pursue criminal charges against the individual.

In response to a question from Representative Winrich, Mr. Erickson said the former secretary-treasurer wrote checks to himself for reimbursement of expenses that could not be supported.

In response to a question from Representative Winrich, Mr. Erickson said the Board of Message is authorized to hire and pay board members or staff to assist with functions such as conducting testing and inspection of massage establishments. He said the secretary-treasurer may be paid for duties associated with the position. He said a standard hourly rate is paid.

AUDITS OF INSTITUTIONS OF HIGHER EDUCATION

Vice Chairman Christmann called on Mr. Nagel who presented the audit report for the University of North Dakota for the years ended June 30, 2003 and 2002. He reviewed the auditor's responses to the committee guidelines and said the report contains five findings of noncompliance with legislative intent. He said the findings relate to the following:

- Receiving approval from the Legislative Assembly or Budget Section to spend gift funds of \$385,000 or more for infrastructure improvements pursuant to NDCC Section 15-10-12.1.

- Recording of deleted or transferred equipment on the fixed asset system.
- Reporting of leases and anticipated leases greater than \$50,000.
- Implementation of a motor pool surcharge.
- Reimbursement of travel expenses.

In response to a question from Representative Skarphol, Ms. Laura Glatt, Vice Chancellor of Administrative Affairs, North Dakota University System office, said there is a cooperative agreement between the Department of Transportation and the state colleges and universities to operate motor pools on the campuses. She said the reimbursement rates received from the Department of Transportation do not cover all the costs incurred by the university to maintain the motor pool. She said the university does not require staff and faculty to conduct routine maintenance such as washing the cars and having the oil changed. She said a surcharge was implemented in order to charge individual departments for these costs and allow for a portion of the costs to be paid from federal funds.

In response to a question from Representative Winrich, Ms. Glatt said state employees that use state motor pool cars from the Bismarck location are responsible for cleaning the cars and are given certificates for oil changes when necessary.

In response to a question from Representative Delzer, Ms. Glatt said the university does not feel it is the best use of faculty or staff time to be responsible for vehicle maintenance. She said these responsibilities are assigned to lower-paid employees.

Mr. Nagel presented the audit report for North Dakota State University for the years ended June 30, 2003 and 2002. He reviewed the auditor's responses to the committee guidelines and said the audit report does not contain any findings or recommendations.

Mr. Nagel presented the audit report for Lake Region State College for the years ended June 30, 2003 and 2002. He reviewed the auditor's responses to the committee guidelines and said the audit report contains three findings of noncompliance with legislative intent relating to reimbursement of travel expenses, implementation of a motor pool surcharge, and preparation of a lease versus purchase analysis.

Mr. Nagel presented the audit report for Williston State College for the years ended June 30, 2003 and 2002. He reviewed the auditor's responses to the committee guidelines and said the audit report does not contain any findings or recommendations.

Ms. Glatt presented information regarding the estimated percentage of tuition and fees that are used to fund academic costs and a historical review of the amount of academic or instruction costs funded by state general fund appropriations. A copy of the information presented is on file in the Legislative Council office.

Ms. Glatt said tuition and fees (net of scholarship allowances) as a percentage of functional expenses,

excluding physical plant functions, averages 37 percent for the North Dakota University System. She said the percentages range from 23 percent at Minot State University - Bottineau to 49 percent at North Dakota State University. She said tuition and fees (net of scholarship allowances) as a percentage of functional expenses, including physical plant functions, averages 33 percent for the North Dakota University System. She said the percentages range from 20 percent at Minot State University - Bottineau to 42 percent at North Dakota State University. She said the significant differences in percentages may be due to enrollment sizes, types of programs offered, scholarship allowances, student mix, and differences in expense classifications.

Ms. Glatt presented information on the current percentage of each institution's appropriations funded from the general fund as compared to tuition. She also presented the targeted percentage rates of funding from state sources and tuition as addressed in the North Dakota University System long-term finance plan.

In response to a question from Senator Krauter, Ms. Glatt said Mayville State University and Valley City State University are currently funded at rates approximately equal to the targeted rates because those institutions receive state funding at a level comparable to their peer institutions. She said other state institutions' funding from state appropriations is significantly less than their peer institutions.

AUDITS OF STATE AGENCIES

Vice Chairman Christmann called on Mr. Ron Tolstad, State Auditor's office, who presented the audit report for the Office of Management and Budget for the years ended June 30, 2003 and 2002. He reviewed the auditor's responses to the committee guidelines and said the audit report contains four findings related to internal control weaknesses, including that Office of Management and Budget:

- Develop a payroll policy to address allowable overtime, other compensation, and the proper authorization of overtime.
- Review the access to the Central Duplicating billing financial information system.
- Implement proper controls over the administration of the purchase care program.
- Develop proper control procedures to comply with NDCC Section 54-44.4-08 relating to use of recycled paper.

Mr. Tolstad said the Office of Management and Budget audit report contained seven findings of noncompliance including:

- North Dakota Century Code Section 54-14-03.1 relating to Budget Section reports.
- Internal Revenue Service regulations regarding withholding on supplemental wages paid.

- State personnel regulations regarding payment of annual leave.
- Emergency Commission request (State Radio).
- North Dakota Century Code Section 54-27-10 relating to appropriation laws (State Radio).
- North Dakota Century Code Section 54-44.4-05 relating to state purchasing guidelines (State Radio).
- State laws governing the accounting for fixed assets (State Radio).

Mr. Tolstad said the audit report included six recommendations for operational improvement relating to improving the state's budgeting process. He said the State Auditor's office studied the current budget policies and practices of the Office of Management and Budget's Budget Office and conducted a best practices review. He said the findings and recommendations relate to the following:

- Budget stabilization fund.
- Enterprise fund transfers.
- Available financial resources.
- Use of one-time revenues.
- Revenue manual.
- Long-term perspective.

Representative Delzer said the Legislative Assembly has provided too much authority relating to the state budget to the executive branch. He said the North Dakota Constitution provides that the Legislative Assembly is responsible for developing the budget of North Dakota.

Representative Winrich said the recommendations for operational improvements should only be addressed by the Legislative Assembly to the extent considered appropriate.

Mr. Nagel presented the audit report for the Department of Corrections and Rehabilitation for the years ended June 30, 2003 and 2002. He reviewed the auditor's responses to the committee guidelines and said the audit report identifies one internal control weakness relating to inadequate controls of the inventory in the pharmacy.

Mr. Welk presented the audit report for the Department of Human Services for the years ended June 30, 2003 and 2002. He reviewed the auditor's responses to the committee guidelines and said the audit report identifies five findings of internal control weaknesses relating to computer access controls, Medicaid management information system (MMIS) duplicate payment controls, pharmaceutical inventory controls, review of child support receivables, and controls of a donation account at the North Central Human Service Center. In addition, the audit report contains one recommendation for operational improvement relating to the regional office automation project. He said one prior audit recommendation relating to MMIS controls was not implemented.

In response to a question from Representative Timm, Mr. Welk said generally Medicaid providers are

honest and return any duplicate payments received. He said it would be cost-prohibitive to add edits for the detection of duplicate payments to the current MMIS system.

In response to a question from Senator Krauter, Mr. Welk said the child support debt adjustments for the 2001-03 biennium totaled approximately \$2.5 million relating to 5,664 adjustments. He said there were 8,000 receipt adjustments totaling approximately \$1 million. He said there were 4,051 debt entries totaling approximately \$8.2 million. Mr. Welk said the audit report included a recommendation that controls be established over child support adjustments to ensure proper oversight and approval and ensure that adjustments are accurate and properly supported. He said adjustments to child support receivables are being made without independent approval or review of support for the adjustment.

Senator Krauter said there needs to be proper documentation to support changes in child support balances. Mr. Welk said documentation is maintained in case files; however, the state payment specialist does not receive the documentation unless it is specifically requested. Senator Krauter asked that acceptance of the Department of Human Services audit be withheld in order for the committee to receive a report from the department at the next meeting regarding its internal control procedures for child support adjustments.

Mr. Nagel presented the audit report for the Children's Services Coordinating Committee for the years ended June 30, 2003 and 2002. He reviewed the auditor's responses to the committee guidelines and said the audit report does not contain any findings or recommendations.

Mr. Nagel presented the audit report for the State Department of Health for the years ended June 30, 2003 and 2002. He reviewed the auditor's responses to the committee guidelines and said the audit report contains two findings of internal control weaknesses relating to computer access control weaknesses over the statewide accounting management and information system and the fixed asset system and procedures surrounding revenue collection. He said the report contains one finding of noncompliance with legislative intent relating to not including a report of expenditures for each local public health unit in the biennial report.

Mr. Nagel presented the audit report for the Water Commission for the years ended June 30, 2003 and 2002. He reviewed the auditor's responses to the committee guidelines and said the audit report identifies one internal control weakness relating to accruing expenditures during the proper accounting period.

Mr. Nagel presented the audit report for the Department of Public Instruction for the years ended June 30, 2003 and 2002. He reviewed the auditor's responses to the committee guidelines and said the audit report contains three findings of noncompliance

with legislative intent relating to overspending the appropriated amount for the grants line item, a conflict between state and federal reporting requirements for public libraries, and the School for the Deaf overspending the amount appropriated for the equipment line item. The audit report contains four recommendations for operational improvement and one internal control weakness relating to computer access controls.

Mr. Nagel presented the audit report for the Department of Career and Technical Education for the years ended June 30, 2003 and 2002. He reviewed the auditor's responses to the committee guidelines and said the audit report does not contain any findings or recommendations.

Mr. Nagel presented the audit report for the Commerce Department for the years ended June 30, 2003 and 2002. He reviewed the auditor's responses to the committee guidelines and said the audit report includes one internal control recommendation relating to implementing a process for calculating and requesting federal HOME program reimbursement.

Mr. Nagel presented the audit report for the Parks and Recreation Department for the years ended June 30, 2003 and 2002. He reviewed the auditor's responses to the committee guidelines and said the audit report does not contain any findings or recommendations.

Mr. Nagel presented the audit report for the Governor's office for the years ended June 30, 2003 and 2002. He reviewed the auditor's responses to the committee guidelines and said the audit report does not contain any findings or recommendations.

Mr. Welk presented the audit report for the Department of Agriculture for the years ended June 30, 2003 and 2002. He reviewed the auditor's responses to the committee guidelines and said the audit report contains two findings of noncompliance with legislative intent relating to overspending the equipment line item and noncompliance with an Emergency Commission request.

In response to a question from Representative Delzer, Mr. Welk said the department received Emergency Commission approval to transfer \$15,000 from the department's operating line to the equipment line to purchase four workstations. He said only two workstations were purchased. He said the remaining unspent fund of \$8,362 was spent on equipment that was not for the purpose requested. He said the Department of Agriculture's response to the recommendation was that they were in compliance with NDCC Section 54-16-03. Mr. Welk said the State Auditor's office will request an Attorney General's opinion regarding the Department of Agriculture's use of funds approved by the Emergency Commission. Representative Delzer asked that the Attorney General's opinion, when issued, be made available to the Legislative Audit and Fiscal Review Committee.

Mr. Nagel presented the audit report for the Insurance Department for the years ended June 30, 2003 and 2002. He reviewed the auditor's responses to the committee guidelines and said the audit report contains one finding of noncompliance with legislative intent relating to incurring expenditures in excess of spending limits for the fire and tornado fund.

Mr. Nagel presented the audit report for the Labor Department for the years ended June 30, 2003 and 2002. He reviewed the auditor's responses to the committee guidelines and said the audit report contains two findings of noncompliance with legislative intent relating to overspending the appropriation for salaries and wages and spending more than 75 percent of the operating expenditures appropriation within the first 18 months of the biennium.

Mr. Nagel presented the audit report for the Aeronautics Commission for the years ended June 30, 2003 and 2002. He reviewed the auditor's responses to the committee guidelines and said the audit report does not contain any findings or recommendations.

It was moved by Senator Andrist, seconded by Senator Krauter, and carried on a roll call vote that, pursuant to NDCC Section 54-35-02.2, the committee accept the following reports presented to the committee:

- **Board of Massage (June 30, 2003 and 2002).**
- **University of North Dakota (June 30, 2003 and 2002).**
- **North Dakota State University (June 30, 2003 and 2002).**
- **Lake Region State College (June 30, 2003 and 2002).**
- **Williston State College (June 30, 2003 and 2002).**
- **Office of Management and Budget (June 30, 2003 and 2002).**
- **Department of Corrections and Rehabilitation (June 30, 2003 and 2002).**
- **Children's Services Coordinating Committee (June 30, 2003 and 2002).**
- **State Department of Health (June 30, 2003 and 2002).**
- **Water Commission (June 30, 2003 and 2002).**
- **Department of Public Instruction (June 30, 2003 and 2002).**
- **Department of Career and Technical Education (June 30, 2003 and 2002).**
- **Commerce Department (June 30, 2003 and 2002).**
- **Parks and Recreation Department (June 30, 2003 and 2002).**
- **Governor's office (June 30, 2003 and 2002).**
- **Department of Agriculture (June 30, 2003 and 2002).**

- **Insurance Department (June 30, 2003 and 2002).**
- **Labor Department (June 30, 2003 and 2002).**
- **Aeronautics Commission (June 30, 2003 and 2002).**
- **Firefighter's Association (April 30, 2003).**
- **Board of Law Examiners (June 30, 2003 and 2002).**
- **Board of Medical Examiners (December 31, 2003 and 2002).**
- **Board of Registration for Professional Engineers and Land Surveyors (June 30, 2003).**
- **State Board of Reflexology (June 30, 2003, 2002, and 2001).**
- **Board of Registration for Professional Soil Classifiers (June 30, 2003).**

INFORMATION SYSTEM AUDIT

Mr. Don LaFleur, State Auditor's office, presented the information system audit of the Department of Corrections and Rehabilitation subject tracking and reporting system (DOCSTARS) for the period January 1, 2003, through December 31, 2003. He said the audit report contains the following three recommendations for the Department of Corrections and Rehabilitation relating to DOCSTARS:

- Perform an annual review of all user accounts to verify that access is appropriate and ensure timely action relating to suspending and closing user accounts.
- Incorporate sufficient edit checks in DOCSTARS.
- Integrate its field services system and its institutional offender system.

Vice Chairman Christmann said because the committee does not have a quorum, action on the acceptance of the DOCSTARS audit report will be delayed until the next meeting.

AUDIT REPORTS FROM ETHANOL PRODUCTION COMPANIES

At the request of Vice Chairman Christmann, the Legislative Council staff distributed a copy of the December 31, 2003, audit report for Alchem, Ltd., LLP. Pursuant to NDCC Section 45-10.1-71, any limited liability partnership that produces agriculture ethyl alcohol or methanol in this state and receives a production subsidy from the state must file an annual audit report with the Legislative Audit and Fiscal Review Committee. The report was filed with the committee pursuant to this section. A copy of the information presented is on file in the Legislative Council office.

COMMITTEE DISCUSSION AND STAFF DIRECTIVES

In response to a question from Representative Delzer, the legislative budget analyst and auditor said the Office of Management and Budget is responsible for certifying the turnback amount to the general fund. He said information will be provided to the committee regarding the verification of turnback of general fund moneys as compared to total general fund appropriations less expenditures.

In response to a question from Representative Delzer, the legislative budget analyst and auditor said if a member of the committee has a question regarding an audit which has been accepted by the Legislative Audit and Fiscal Review Committee, the legislator can either contact the department or the State Auditor's office or formally request the information during a meeting of the Legislative Audit and Fiscal Review Committee.

In response to a question from Representative Skarphol, the legislative budget analyst and auditor said pursuant to a request from the Budget Section, state agencies and institutions are asked to present a summary of assets owned as part of budget tours. Representative Skarphol said budget tours are not

conducted for all agencies. He said the Department of Transportation owns property in Fargo, near West Acres Shopping Center, that is estimated to be worth \$2 million. He asked that an analysis be prepared of assets owned by all state agencies, including the value and use of those assets. Vice Chairman Christmann said the Legislative Council staff can work with Chairman Wald regarding the request for information.

The meeting was adjourned subject to the call of the chair at 4:45 p.m.

Donald J. Wolf
Senior Fiscal Analyst

Jim W. Smith
Legislative Budget Analyst and Auditor

ATTACH:2