

# NORTH DAKOTA LEGISLATIVE COUNCIL

Minutes of the

## LEGISLATIVE AUDIT AND FISCAL REVIEW COMMITTEE

Wednesday, August 31, 2005  
Roughrider Room, State Capitol  
Bismarck, North Dakota

Representative Francis J. Wald, Chairman, called the meeting to order at 8:30 a.m.

**Members present:** Representatives Francis J. Wald, Ole Aarsvold, Merle Boucher, RaeAnn G. Kelsch, Andrew G. Maragos, David Monson, Chet Pollert, Bob Skarphol, Blair Thoreson, Mike Timm; Senators Bill L. Bowman, Randel Christmann, Jerry Klein, Judy Lee, Tim Mathern

**Members absent:** Representatives Jeff Delzer, Earl Rennerfeldt

**Others present:** See attached appendix

### LEGISLATIVE COUNCIL SUPPLEMENTARY RULES OF OPERATION AND PROCEDURE

At the request of Chairman Wald, the legislative budget analyst and auditor reviewed the [Supplementary Rules of Operation and Procedure of the North Dakota Legislative Council](#) for the 2005-07 biennium.

### COMMITTEE DUTIES AND RESPONSIBILITIES

At the request of Chairman Wald, the Legislative Council staff reviewed a memorandum entitled [Legislative Audit and Fiscal Review Committee - Statutory Duties and Responsibilities for the 2005-06 Interim - Recommendations and Requests Made During Previous Interims](#). The Legislative Audit and Fiscal Review Committee is a statutory committee of the Legislative Council. North Dakota Century Code (NDCC) Section 54-35-02.1 provides that the committee is created to:

- Study and review the financial transactions of the state.
- Assure the collection of revenues and the expenditures of money are in compliance with law, legislative intent, and sound financial practices.
- Provide the Legislative Assembly with formal, objective information on revenue collections and expenditures.

In addition, the committee is assigned the following duties and responsibilities for the 2005-07 biennium:

1. **State Fair Association** - Receive annual audit reports from the State Fair Association, pursuant to NDCC Section 4-02.1-18.

2. **Ethyl alcohol and methanol producers** - Receive annual audit reports from any corporation that produces agricultural ethyl alcohol or methanol in this state and which receives a production subsidy from the state, pursuant to NDCC Section 10-19.1-152; receive annual audit reports from any limited liability company that produces agricultural ethyl alcohol or methanol in this state and which receives a production subsidy from the state, pursuant to Section 10-32-156; and receive annual audit reports from any limited partnership that produces agricultural ethyl alcohol or methanol in this state and which receives a production subsidy from the state, pursuant to Section 45-10.2-115.
3. **Department of Human Services accounts receivable** - Receive annual reports on the status of accounts receivable for the Department of Human Services and Developmental Center at Westwood Park, Grafton, pursuant to NDCC Sections 25-04-17 and 50-06.3-08.
4. **Low-risk incentive fund** - Receive annual audit reports and economic impact reports from the North Dakota low-risk incentive fund. North Dakota Century Code Section 26.1-50-05 provides for the audit report to be submitted to the Legislative Council, which has assigned the responsibility to this committee.
5. **Stockmen's Association** - Receive a biennial audit report from the North Dakota Stockmen's Association. North Dakota Century Code Section 36-22-09 provides for the audit report to be submitted to the Legislative Council. The Legislative Council assigned the responsibility to this committee.
6. **Job Service North Dakota** - Receive a performance audit report, upon the request of the committee, for Job Service North Dakota, pursuant to NDCC Section 52-02-18.  
The 2005 Legislative Assembly approved Senate Bill No. 2085 which changed the frequency of Job Service North Dakota's performance audit from biennial to as requested by the Legislative Audit and Fiscal Review Committee.

7. **Performance audits** - The State Auditor is to conduct or provide for performance audits of state agencies as determined necessary by the State Auditor or this committee, and the State Auditor must obtain approval from this committee prior to hiring a consultant to assist with conducting a performance audit, pursuant to NDCC Section 54-10-01.
  8. **Frequency of audits** - Determine the frequency of audits or reviews of state agencies, pursuant to NDCC Section 54-10-01.
  9. **Political subdivisions** - Determine if the State Auditor is to perform audits of political subdivisions on a more frequent basis than once every two years, pursuant to NDCC Section 54-10-13, and direct the State Auditor to audit or review the accounts of any political subdivision, pursuant to Section 54-10-15.
  10. **Study and review audit reports** - Pursuant to NDCC Section 54-35-02.2, the committee is charged with the following responsibilities:
    - a. To study and review audit reports selected by the committee from those submitted by the State Auditor.
    - b. To confer with the State Auditor regarding the audit reports reviewed by the committee.
    - c. As necessary, to confer with representatives of state departments, agencies, and institutions audited in order to obtain information regarding fiscal transactions and governmental operations.
  11. **Workforce Safety and Insurance** - Receive annual reports from the director of Workforce Safety and Insurance and the chairman of the Workforce Safety and Insurance Board of Directors, pursuant to NDCC Section 65-02-03.3, and receive reports from the director of Workforce Safety and Insurance, the chairman of the Workforce Safety and Insurance Board of Directors, and the auditor regarding the biennial performance audit of Workforce Safety and Insurance, pursuant to Section 65-02-30.
  12. **Information Technology Department** - Receive annual reports on state information technology projects and plans, pursuant to NDCC Section 54-59-19.
3. Request a performance audit be conducted, as deemed necessary by this committee, for Job Service North Dakota.
  4. Receive the biennial performance audit of Workforce Safety and Insurance.
  5. Direct the Legislative Council staff to send correspondence, as deemed necessary, to each agency that has not complied with previous audit recommendations requesting the agency to appear before the Legislative Audit and Fiscal Review Committee to explain the reason for noncompliance with audit recommendations or steps taken to address recommendations.
  6. Receive annual reports on state information technology projects and plans.
  7. Receive annual reports on the status of accounts receivable for the Department of Human Services and Developmental Center at Westwood Park, Grafton.
  8. Receive annual audit reports from any corporation, limited partnership, or limited liability company that produces ethyl alcohol or methanol in this state and which receives a production subsidy from the state.
  9. Develop recommendations and related bill drafts.
  10. Prepare the final report for submission to the Legislative Council.

### CONTINUING APPROPRIATION STUDY

The Legislative Council staff said 2005 House Concurrent Resolution No. 3036 provides for a study of state agency and institution continuing appropriation authority. Continuing appropriations are provided by a statutory authorization that remains in force or can be carried on from biennium to biennium permitting state agencies, boards, or institutions to incur obligations and make payment for specified purposes or uses. The North Dakota Century Code contains many examples of continuing appropriations, which are typically created by using phrases such as "standard appropriation," "continuing appropriation," or "revolving fund."

In response to a question from Representative Skarphol, the legislative budget analyst and auditor said a state agency could add an employee position that is not authorized by the Legislative Assembly if that position is funded by a continuing appropriation. He said the "off-budget" position may be eligible for state employee benefits. If the continuing appropriation is discontinued, the employee position would also be discontinued, unless provided for through another appropriation.

The Legislative Council staff presented the following proposed action plan for the committee to consider in fulfilling its duties to study state agency and institution continuing appropriations:

The Legislative Council staff presented the following proposed action plan for the committee to consider in fulfilling its statutory duties:

1. Receive audit reports prepared by the State Auditor's office and independent auditors.
2. Receive performance audit reports as determined necessary by the State Auditor or this committee.

1. Request selected state agencies and institutions to provide information on statutory authority for continuing appropriation authority within the agency or institution; justification for continuing the authority; and related expenditures, revenues, and fund balance for the audit period and projected for following years.
2. Receive information from any interested organizations, entities, and individuals regarding the study of continuing appropriation authority.
3. Review the continuing appropriations summary report prepared by the Office of Management and Budget for the Appropriations Committees of the 2005 Legislative Assembly.
4. Develop recommendations and related bill drafts.
5. Prepare the final report for submission to the Legislative Council.

### **AUDIT PROCESS FOR STATE AGENCIES**

Chairman Wald called on Mr. Ed Nagel, State Auditor's office, who reviewed a document entitled *The Audit Process for State Agencies and the Relationship Between the Office of the State Auditor and the Legislative Audit and Fiscal Review Committee*. A copy of the information presented is on file in the Legislative Council office. Mr. Nagel said the purpose of the financial statement audit is to express an opinion on whether the financial statements are presented fairly in all material respects. He said the audited entity's management is responsible for the financial statements. He said the State Auditor's office performs annual financial statements, biennial financial-related operational audits, a biennial audit of the state's federal financial assistance, and performance audits.

In response to a question from Representative Wald, Mr. Nagel said the objective of performance audits is to improve program operations and facilitate decisionmaking for parties with oversight responsibility.

In response to a question from Representative Maragos, Mr. Nagel said performance audits are intended to improve the overall performance of an agency or institution; however, the State Auditor's office does not have the resources to conduct a performance audit of all state agencies and institutions.

In response to a question from Representative Skarphol, Mr. Nagel said the Legislative Council is responsible for selecting the firm to conduct the audit of the State Auditor's office.

### **VETERANS HOME PERFORMANCE AUDIT - FOLLOWUP REPORT**

Chairman Wald called on Mr. Gordy Smith, State Auditor's office, who presented the followup report on the Veterans Home performance audit. He said 25 prior audit recommendations were fully implemented, 15 prior audit recommendations were partially implemented, and 6 were determined to be not implemented.

In response to a question from Representative Wald, Mr. Gordy Smith said the Administrative Committee on Veterans Affairs is a 15-member committee with 3 members representing each of the 5 major veteran organizations in the state. He said the State Auditor's office recommended that the committee size be reduced in order to better react to the needs of veterans.

In response to a question from Representative Wald, Mr. Gordy Smith said the members of the Administrative Committee on Veterans Affairs are paid per diem from the veterans' postwar trust fund.

In response to a question from Representative Aarsvold, Mr. Neal Asper, Administrator, Veterans Home, said he is a fully licensed nursing home administrator, as was the previous administrator.

Senator Mathern said the members of the Administrative Committee on Veterans Affairs and the employees of the Veterans Home should be commended for their hard work in implementing the performance audit recommendations.

In response to a question from Senator Bowman, Mr. Gordy Smith said the Administrative Committee on Veterans Affairs has taken a very active role in the operations of the Veterans Home and is committed to implementing and following the performance audit recommendations.

In response to a question from Representative Wald, Mr. Gordy Smith said he believes the Veterans Home has taken significant steps to implement the performance audit recommendations and said another followup by the State Auditor's office is not necessary.

In response to a question from Representative Aarsvold, Mr. Gordy Smith said there has been a significant change in membership of the Administrative Committee on Veterans Affairs since the performance audit was conducted.

Mr. Asper said the Veterans Home has improved its working relationship with the Office of Management and Budget, State Auditor's office, and Attorney General's office. He said previous individuals in management positions at the Veterans Home lacked necessary qualifications and leadership abilities. He said there have been many employee and policy changes to improve the management of the Veterans Home.

In response to a question from Representative Wald, Mr. Asper said the Veterans Home currently has 118 total residents--38 residents in skilled care and 80 residents in basic care.

In response to a question from Representative Skarphol, Mr. Rudy Jenson, Chairman, Administrative Committee on Veterans Affairs, said the seven-member governing board responsible for overseeing administration of the Veterans Home is appointed by the chairman and secretary of the Administrative Committee on Veterans Affairs, subject to ratification by a majority of the administrative committee. He said approximately three or four members of the governing board are also members of the administrative committee.

Senator Lee said the Budget Committee on Health Care toured the Veterans Home during the 2003-04 interim and concluded that there have been many operational improvements at the Veterans Home.

## **NORTH DAKOTA RACING COMMISSION AUDIT**

Mr. Gordy Smith presented information regarding the North Dakota Racing Commission audit report for the fiscal years ended June 30, 2004 and 2003. A copy of the information presented is on file in the Legislative Council office. He said the audit report was originally presented to the Legislative Audit and Fiscal Review Committee during the April 5, 2005, meeting.

Mr. Gordy Smith said during the April 2005 meeting, the committee asked for the terms of repayment, if required, of \$1 million of city of Fargo tax increment financing district funds provided to assist in the construction of the racetrack in Fargo (the North Dakota Horse Park). He said a total of 114.5 acres of farmland was made available by Sheyenne Development LLP to initiate the process of developing the North Dakota Horse Park for a cost of \$250,000, which was paid by the city of Fargo. He said 14.5 acres of the land was set aside and deeded to North Dakota State University Development Foundation. He said 65 acres were leased on a 99-year lease to the North Dakota Horse Park Foundation with the responsibility of maintaining the racetrack. He said Horse Race North Dakota (a nonprofit organization serving interests of horsemen) has a 99-year lease to the land on which the grandstand, bathrooms, parking lots, temporary offices, and adjacent grounds are located. He said the area surrounding the 114.5 acres provided for the North Dakota Horse Park consists of undeveloped property. He said the tax increment financing terms provide that if there is a total of \$5 million of development on the surrounding property by February 2007, the \$1 million city of Fargo tax increment financing district funds do not have to be repaid. He said he believes the city of Fargo may levy a proportional assessment against the North Dakota Horse Park for an amount up to \$1 million based on the amount of development, if less than \$5 million.

In response to a question from Senator Christmann, Mr. Gordy Smith said he is not aware of

the exact boundaries or acreage of the referred to surrounding property but does not believe any of the area surrounding the North Dakota Horse Park has been developed.

In response to a question from Representative Timm, Mr. Gordy Smith said the North Dakota Racing Commission is not responsible for repaying the city of Fargo tax increment financing district funds.

In response to a question from Representative Wald, Mr. Gordy Smith said the North Dakota Racing Commission operates three separate funds--the breeders fund, which is used to provide additional funds to North Dakota-born horses that race and win, place, or show in a race at a North Dakota track; the purse fund, which is used to provide additional funds to North Dakota racetracks for purses for their live races; and the promotion fund, which is for promotion of horse racing and a variety of other functions, including providing funding for construction of the North Dakota Horse Park.

Representative Boucher said architects estimated that it would cost \$475,000 to construct the racetrack in Fargo as compared to actual costs of \$2,234,000. He said architects estimated it would cost \$30,000 to install underground utilities as compared to current estimated actual costs of \$458,000. He said the committee should ask representatives of the North Dakota Horse Park to provide an explanation for the large differences in actual costs as compared to the original estimates.

In response to a question from Representative Kelsch, Mr. Gordy Smith said the State Auditor's office authority to audit the North Dakota Horse Park is limited to the use of funds provided by the North Dakota Racing Commission. Senator Mathern said the committee should request the North Dakota Horse Park to voluntarily provide information and answers to questions regarding the operations and cost of the racetrack.

In response to a question from Representative Skarphol, Mr. Gordy Smith said based on an unaudited income statement, Horse Race North Dakota's total 2004 revenues were \$1,013,136, of which \$718,400 was from North Dakota Racing Commission grants. He said based on projected revenues and expenditures, the promotion fund has approximately three years of funding remaining and the purse and breeders fund have approximately five years of funding remaining. He said Horse Race North Dakota would have difficulty continuing without financial support from the North Dakota Racing Commission.

In response to a question from Representative Wald, Mr. Gordy Smith said the North Dakota Racing Commission is not legally obligated to provide any additional funding to the North Dakota Horse Park.

Mr. Gordy Smith said based on informal discussions with the Attorney General's office, the North Dakota Racing Commission most likely would not be

liable for any debts incurred by the North Dakota Horse Park.

Mr. Gordy Smith said based on informal discussions with the Attorney General's office and the Risk Management Division of the Office of Management and Budget, the state may incur liability if sued by someone injured at a licensed racetrack, depending on if the state had prior knowledge of any safety issues relating to the racetrack.

Chairman Wald called on Mr. James Boehm, Chairman, North Dakota Racing Commission, who commented on the status of the North Dakota Racing Commission and the North Dakota Horse Park. Mr. Boehm said it is the goal of the North Dakota Horse Park to be self-sufficient. He said the "handle" or amount wagered in North Dakota has increased over the last few months. He said the committee should ask for information from the North Dakota Horse Park regarding the cost of the Fargo racetrack facilities and use of funds provided by the North Dakota Racing Commission. He said only funds from the promotion fund were provided for construction of the racetrack.

In response to a question from Representative Timm, Mr. Boehm said approximately 95 percent of the total amount wagered on horse racing in North Dakota is on simulcast racing and 5 percent is on live in-state horse racing.

In response to a question from Representative Kelsch, Mr. Boehm said there are 18 days of live racing scheduled annually at the North Dakota Horse Park.

Representative Kelsch said according to the North Dakota Horse Park web site, the Fargo racetrack is currently estimated to cost over \$10 million.

In response to a question from Representative Kelsch, Mr. Boehm said the daily operations of the North Dakota Racing Commission have been overseen by an administrative assistant and himself since June 2005, when the director was fired. He said he and the Office of Management and Budget approve the North Dakota Racing Commission expenditures.

In response to a question from Representative Boucher, Mr. Boehm said he would provide the committee with information regarding the potential liability of commissioners and the state in the event of negligence of the North Dakota Racing Commission.

**It was moved by Representative Boucher, seconded by Senator Lee, and carried on a roll call vote that the Legislative Audit and Fiscal Review Committee request Horse Race North Dakota and the North Dakota Horse Park Foundation to provide a cost report for construction and operation of the North Dakota Horse Park and the reasons for actual costs exceeding original estimates.** Representatives Wald, Aarsvold, Boucher, Kelsch, Maragos, Monson, Pollert, Skarphol, Thoreson, and Timm and Senators Bowman,

Christmann, Klein, Lee, and Mathern voted "aye." No negative votes were cast.

**It was moved by Representative Skarphol, seconded by Representative Kelsch, and carried on a roll call vote that the Legislative Audit and Fiscal Review Committee request information regarding the identity of the board members, stockholders, or individuals associated with the North Dakota Horse Park Foundation, Horse Race North Dakota, and Sheyenne Development LLP; the current status and plans for development of the land surrounding the North Dakota Horse Park and the intent of the city of Fargo regarding requiring repayment of \$1 million of tax increment financing district funds; and the financial status of other states' horse racing tracks, including information on other forms of onsite entertainment or businesses operating on track facilities and whether the racetrack operations are subsidized by these businesses or any other sources.** Representatives Wald, Aarsvold, Boucher, Kelsch, Maragos, Monson, Pollert, Skarphol, Thoreson, and Timm and Senators Bowman, Christmann, Klein, Lee, and Mathern voted "aye." No negative votes were cast.

**It was moved by Representative Wald, seconded by Representative Kelsch, and carried on a roll call vote that the Legislative Audit and Fiscal Review Committee ask the chairman of the Legislative Council to send a letter encouraging the North Dakota Racing Commission to determine whether the horse racing tracks licensed by the North Dakota Racing Commission have liability insurance that extends coverage to the state of North Dakota and, if not, request the respective horse racing tracks to obtain a certificate of insurance extending liability insurance coverage to the state of North Dakota for a minimum amount of \$1 million or for the stated amount of the race track's liability insurance coverage if that amount is greater than \$1 million.** Representatives Wald, Boucher, Kelsch, Maragos, Monson, Pollert, Skarphol, Thoreson, and Timm and Senators Bowman, Christmann, Klein, and Lee voted "aye." Representative Aarsvold and Senator Mathern voted "nay."

In response to a question from Senator Mathern, the legislative budget analyst and auditor said the process for an interim committee to encourage a state agency, in this case the North Dakota Racing Commission, to follow direction from the committee is through the issuance of a letter signed by the chairman of the Legislative Council.

Senator Mathern said the committee should receive cost information before directing that insurance coverage be obtained. Representative Wald said it is common in a landlord-tenant relationship to add another entity as an additional certificate of insurance.

Mr. Boehm said he believes the North Dakota Horse Park has liability insurance and that a certificate of insurance extending coverage to the state of North Dakota could become a part of the licensing requirement.

### AUDITS OF STATE AGENCIES

Chairman Wald called on Ms. Barb Aasen, Eide Bailly LLP, Certified Public Accountants, who presented the audit report for Job Service North Dakota for the years ended June 30, 2004 and 2003. She said the report contains an unqualified opinion and does not contain any findings or recommendations relating to the financial statements. She said the report identified one finding for federal awards programs relating to including a disclosure for service contracts in excess of \$100,000.

Mr. Joel Thomsen, Eide Bailly LLP, Certified Public Accountants, presented the audit report for Workforce Safety and Insurance for the years ended June 30, 2004 and 2003. He said the report contains an unqualified opinion and contains five findings and recommendations relating to documenting all equipment locations, proper documentation for employee expense reimbursements, improving case reserving practices, updating the access approval process within the claims management system, and rectifying data integrity issues within the claims management system.

In response to a question from Senator Mathern, Mr. Darrell Lingle, Eide Bailly LLP, Certified Public Accountants, said the auditing fee for the Workforce Safety and Insurance audit was \$38,000.

Ms. Aasen presented the audit report for the Public Employees Retirement System for the years ended June 30, 2004 and 2003. She said the report contains an unqualified opinion and does not contain any findings or recommendations.

Ms. Aasen presented the audit report for the State Fair Association for the years ended September 30, 2004 and 2003. She said the report contains an unqualified opinion and one internal control finding relating to segregation of accounting duties. She said the report contains one finding of noncompliance with legislative intent relating to cash deposited at a local financial institution rather than the Bank of North Dakota.

In response to a question from Representative Wald, Mr. Gerald Iverson, Manager, State Fair Association, said a provision of the arena maintenance and operations agreement requires related State Fair funds to be deposited in a local bank. He said the arena was constructed with state, city, and county funds and the governing board of the arena is represented equally by individuals from each form of government. He said even though the State Fair Association manages the arena, the governing board has control of the funds. Representative Timm said the State Fair Association should have legislation

introduced to provide an exception to the State Fair Association from the law requiring these funds to be deposited in the Bank of North Dakota.

Mr. Greg Honl, Eide Bailly LLP, Certified Public Accountants, presented the audit report for the Bank of North Dakota for the years ended December 31, 2004 and 2003. He said the report contains an unqualified opinion and does not contain any findings or recommendations.

Mr. Eric Hardmeyer, President, Bank of North Dakota, said the 2005 Legislative Assembly provided for the minimum required capital balance for the Bank of North Dakota to be increased from \$140 million to \$150 million.

Mr. Honl presented the audit report for the Bank of North Dakota information system procedures for the year ended December 31, 2004. He reviewed the operational recommendations relating to risk assessment, user access, and protection of data.

Ms. Aasen presented the audit report for the Municipal Bond Bank for the years ended December 31, 2004 and 2003. She said the report contains an unqualified opinion and one internal control finding relating to segregation of accounting duties.

Chairman Wald called on Mr. John Mongeon, Brady, Martz & Associates, P.C., Certified Public Accountants, who presented the audit report for the Retirement and Investment Office for the years ended June 30, 2004 and 2003. He said the report contains an unqualified opinion and does not contain any findings or recommendations.

Mr. Mongeon said the actuary for the Teachers' Fund for Retirement has determined the fund's unfunded actuarial accrued liability is approximately \$355 million as of June 30, 2004. He said the actuary has determined that the current statutory contribution rates are insufficient to amortize the unfunded actuarial accrued liability over any period of time, based on the current actuarial assumptions, unless there are sufficient actuarial gains in the future to offset the recent investment losses.

Mr. Steve Cochrane, Executive Director/Investment Director, Retirement and Investment Office, said the fiscal year ended June 30, 2005, investment return for the Teachers' Fund for Retirement was 13.5 percent as compared to the actuarial assumption of 8 percent. However, he said, the fund is operated on a five-year "smoothing" basis and actuarial losses for the years ended June 30, 2001, 2002, and 2003 are included in determining the actuary investment return.

In response to a question from Representative Skarphol, Mr. Cochrane said the Public Employees Retirement System fund had an investment return in excess of 14 percent for the fiscal year ended June 30, 2005, and is very close to being fully funded.

The committee recessed for lunch from 12:05 to 1:00 p.m.

Mr. Mongeon presented the audit report for the Housing Finance Agency for the years ended June 30, 2004 and 2003. He said the report contains an unqualified opinion and does not contain any findings or recommendations.

Mr. Mongeon presented the audit report for the Board of University and School Lands for the years ended June 30, 2004 and 2003. He said the report contains an unqualified opinion and does not contain any findings or recommendations.

### **BANK OF NORTH DAKOTA BUILDING PROJECT STATUS**

Chairman Wald called on Mr. Hardmeyer who commented on the current status of the planned new Bank building. Mr. Hardmeyer said the 2005 Legislative Assembly authorized the Bank of North Dakota to use \$11 million of special funds from the Bank's assets to construct a new three-story Bank building consisting of a total of 60,000 square feet. He said the Industrial Commission is to advertise for bids for the new Bank building and solicit alternate bids which would allow footings to be included to allow for up to three additional floors. He said the legislation provides that the Industrial Commission is to make the final decision for the location of the new Bank building and may proceed with construction with the additional footings upon approval of the Emergency Commission and Budget Section.

Mr. Hardmeyer said the Bank of North Dakota has solicited public opinion regarding the possible locations for the Bank building. He said the Bank is currently considering 15 or 16 different locations in the Bismarck/Mandan area. He said accessibility, parking, cost, and ability to expand at the location will be major factors in determining the location.

In response to a question from Representative Timm, Mr. Hardmeyer said he is not aware of any statutory or constitutional provisions that require the Bank of North Dakota to be located in Bismarck.

In response to a question from Representative Kelsch, Mr. Hardmeyer said the Industrial Commission asked that the Bank of North Dakota recommend more than one site for consideration. He said the Bank of North Dakota determined it would not be appropriate for the Bank to accept incentives to locate in any particular city or location.

In response to a question from Representative Wald, Mr. Hardmeyer said the Bank of North Dakota has budgeted approximately \$1.5 million for land acquisition. He said if the Bank decides to rebuild at its present location, the \$1.5 million will be applied to temporary relocation and demolition costs. Mr. Hardmeyer said it is likely that demand for building supplies as a result of damage caused by Hurricane Katrina will have a significant impact on construction costs.

In response to a question from Representative Monson, Mr. Hardmeyer said it is possible the Bank of

North Dakota may consider selling the portion of the Bank building that used to be a grocery store separately from the Bank tower. He said the Bank of North Dakota may also consider doing a land "swap."

### **NORTH DAKOTA STOCKMEN'S ASSOCIATION AUDIT**

Chairman Wald called on Ms. Rhonda Mahlum, Mahlum and Goodhart, P.C., Certified Public Accountants, who presented the audit report of the North Dakota Stockmen's Association for the years ended December 31, 2004 and 2003. She said the report contains an unqualified opinion and includes four internal control findings relating to segregation of duties, bank balances in excess of Federal Deposit Insurance Corporation (FDIC) coverage of \$100,000, signing of board minutes, and reconciliation of the estray account.

### **AUDITS OF STATE AGENCIES**

Chairman Wald called on Mr. Ron Tolstad, State Auditor's office, who presented the audit report of the North Dakota lottery for the year ended June 30, 2004. He reviewed the auditor's responses to the committee guidelines and said the report identifies one internal control weakness relating to computer access privileges for the games management system. He said the report contains one finding of noncompliance with legislative intent relating to depositing all revenues into the operating fund, pursuant to NDCC Section 53-12-19.

In response to a question from Representative Aarsvold, Ms. Kathy Roll, Attorney General's office, said the North Dakota lottery operated on a continuing appropriation for the 2003-05 biennium. However, she said, the 2005 Legislative Assembly provided a specific 2005-07 biennium appropriation, primarily for administrative costs of the North Dakota lottery.

In response to a question from Representative Timm, Mr. Chuck Keller, North Dakota lottery director, Attorney General's office, said the multistate lottery reserve pools is money set aside for extraordinary circumstances, such as if there is a winning lottery ticket that, through error, is not recognized by the computer system. He said the North Dakota reserve assessment was based on the state's population for the first year of involvement in the multistate lottery and will be based on actual sales for all following years.

Mr. Nagel presented the audit report of the Game and Fish Department for the years ended June 30, 2004 and 2003. He reviewed the auditor's responses to the committee guidelines and said the report does not contain any findings or recommendations.

Mr. Nagel presented the audit report of the Department of Veterans Affairs for the years ended June 30, 2004 and 2003. He reviewed the auditor's responses to the committee guidelines and said the report contains one finding of noncompliance with legislative intent relating to preparation of minutes for

subcommittee meetings. He said two prior audit recommendations were determined not to be implemented.

Mr. Nagel presented the audit report of the Seed Department for the years ended June 30, 2004 and 2003. He reviewed the auditor's responses to the committee guidelines and said the report contains one finding of noncompliance with legislative intent relating to conflicting sections in the North Dakota Century Code.

In response to a question from Senator Klein, the legislative budget analyst and auditor said the conflicting North Dakota Century Code sections referred to in the Seed Department audit were not addressed by the 2005 Legislative Assembly.

Mr. Paul Welk, State Auditor's office, presented the audit report of the Attorney General's office for the years ended June 30, 2004 and 2003. He reviewed the auditor's responses to the committee guidelines and said the report contains two findings of noncompliance with legislative intent relating to developing guidelines for the establishment and operation of block house programs and depositing of background check revenues. He said the report identifies one internal control weakness relating to payroll system access controls. He said the report contains three recommendations for operational improvement relating to implementation of a Medicaid fraud control unit; improvements for the sex offender web site, assessment/registration requirements, and notification/tracking of sex offenders; and procedures for receipting, reviewing, and processing license applications.

Representative Thoreson said hopefully in the future the Attorney General's office can reinstate the block house program.

Mr. Welk presented the audit report of the Information Technology Department for the years ended June 30, 2004 and 2003. He reviewed the auditor's responses to the committee guidelines and said the report contains one finding of noncompliance with legislative intent relating to overspending 75 percent of the operating expenses line item within the first 18 months of the biennium. He said the report identifies one internal control weakness relating to computer access controls.

Mr. Nagel presented the audit report of the University System office for the years ended June 30, 2004 and 2003. He reviewed the auditor's responses to the committee guidelines and said the report does not contain any findings or recommendations.

Mr. Welk presented the audit report of the Highway Patrol for the years ended June 30, 2004 and 2003. He reviewed the auditor's responses to the committee guidelines and said the report identifies three internal control weaknesses relating to payroll controls, controls for receipt and recording of federal funds, and controls for approval of bank reconciliations. He said the report contains four recommendations for

operational improvement relating to use of purchase cards for small dollar items, electronically transferring funds in clearing accounts to the Bank of North Dakota, grant monitoring procedures, and maximizing use of federal funds. He said three prior audit recommendations were not implemented.

Mr. Welk presented the audit report of the Secretary of State's office for the years ended June 30, 2004 and 2003. He reviewed the auditor's responses to the committee guidelines and said the report contains one recommendation for operational improvement relating to creating a one-stop online business registration process.

Mr. Nagel presented the audit report of the Department of Financial Institutions for the years ended June 30, 2004 and 2003. He reviewed the auditor's responses to the committee guidelines and said the report contains one recommendation for operational improvement relating to additional use of online processing of license applications and renewals.

Mr. Nagel presented the audit report of the Securities Department for the years ended June 30, 2004 and 2003. He reviewed the auditor's responses to the committee guidelines and said the report contains two findings of noncompliance with legislative intent relating to overpayment of per diem meal rate allowance for out-of-state travel and noncompliance with state purchasing guidelines.

Mr. Nagel presented the audit report of the Adjutant General for the years ended June 30, 2004 and 2003. He reviewed the auditor's responses to the committee guidelines and said the report contains one finding of noncompliance with legislative intent relating to fees charged by State Radio Communications for services provided. He said the report identifies two internal control weaknesses relating to fixed asset internal control procedures and controls surrounding recording of expenditures in the proper accounting period. He said one prior audit recommendation was not implemented.

Mr. Nagel presented the audit report of the State Historical Society for the years ended June 30, 2004 and 2003. He reviewed the auditor's responses to the committee guidelines and said the report contains one finding of noncompliance with legislative intent relating to accounting for capital assets. He said the report identifies one internal control weakness relating to state purchase card controls.

In response to a question from Senator Lee, Mr. Nagel said generally accepted accounting principles provide for the depreciation of art collections with certain exceptions for "fine" art.

Mr. Nagel presented the audit report of the Protection and Advocacy Project for the years ended June 30, 2004 and 2003. He reviewed the auditor's responses to the committee guidelines and said the report contains one recommendation for operational improvement relating to use of purchase cards for small-dollar purchases.

In response to a question from Representative Wald, Mr. Nagel said the Office of Management and Budget provides instructions to state agencies regarding the use of purchase cards.

Mr. Nagel presented the audit report of the Indian Affairs Commission for the years ended June 30, 2004 and 2003. He reviewed the auditor's responses to the committee guidelines and said the report contains one finding of noncompliance with legislative intent relating to conducting employee performance reviews. He said the report contains one recommendation for operational improvement relating to use of purchase cards for small-dollar purchases.

### **CONNECTND HUMAN RESOURCE MANAGEMENT SYSTEM INFORMATION SYSTEM AUDIT**

Mr. Don LaFleur, State Auditor's office, presented the Office of Management and Budget ConnectND human resource management system (HRMS) information system audit report for the year ended December 31, 2004. He said ConnectND HRMS is used to maintain and process payroll records for employees of the state of North Dakota and the North Dakota University System. He said ConnectND HRMS was selected for this audit because it is considered a high-risk information system. He said "high-risk" does not necessarily indicate problems with the system, but indicates a higher potential for significant problems to occur.

Mr. LaFleur said the audit report contains seven internal control findings relating to inadequate user roles for state agency personnel, inappropriate access to sensitive information, default accounts not locked in a timely manner to prevent unauthorized access, excess superuser access, ability of employees to update their own payroll data, invalid chart field information processed by the system, and inadequate policies and procedures for the payroll process.

In response to a question from Senator Christmann, Mr. LaFleur said North Dakota State University has been experiencing problems with its student finance data base, which is not part of the ConnectND HRMS.

### **COMPREHENSIVE ANNUAL FINANCIAL REPORT**

Ms. Eileen Holwegner, Office of Management and Budget, presented the Comprehensive Annual Financial Report (CAFR) for the state of North Dakota for the fiscal year ended June 30, 2004. Ms. Holwegner reviewed the information contained in the report and a supplemental report entitled *Interim 2003-05 Biennium Budget and Actual Detail*. Copies of both reports are on file in the Legislative Council office.

In response to a question from Senator Lee, Ms. Holwegner provided information to the committee

regarding why columns do not total in the statement of net assets presented in the management discussion and analysis section of the CAFR. She indicated that the balances do not total because internal balances (the amount due to and from other state funds) were "eliminated" to present a "consolidated balance sheet." She said she would be willing to provide further explanation to the committee during the next meeting.

Mr. Tolstad presented the State Auditor's office report on the state of North Dakota internal control and compliance report for the fiscal year ended June 30, 2004. The report indicates that the State Auditor's office has audited the general purpose financial statements for the state of North Dakota for the year ended June 30, 2004. He said the report contains two internal control findings relating to lack of financial reporting controls for the preparation of the state's financial statements and lack of proper payroll access controls.

In response to a question from Representative Boucher, Mr. Tolstad said an error rate of 6 percent was discovered relating to adjustments needed to report the state's balances and activities in accordance with generally accepted accounting principles. He said several factors contributed to the state's unacceptable generally accepted accounting principles adjustment error rate. He said the most significant factor related to resources being diverted to the implementation of the state's new accounting system (ConnectND) while the adjustments and the state's financial statements were being prepared.

In response to a question from Senator Bowman, Mr. Tolstad said additional audit testing was necessary because of the number of errors discovered; however, an unqualified opinion was issued for the CAFR.

### **STATE OF NORTH DAKOTA SINGLE AUDIT REPORT**

Mr. Gordy Smith presented the statewide single audit report for the years ended June 30, 2004 and 2003. He said the statewide single audit is the state's audit of all federal funds received by state agencies and institutions during fiscal years 2004 and 2003. He reviewed the different sections of the report which include selected statistical data, independent auditor's reports, schedule of expenditures of federal awards, schedule of findings and questioned costs, and a summary schedule of prior audit findings. He said the report contains 26 internal control and compliance findings.

### **NORTH DAKOTA UNIVERSITY SYSTEM ANNUAL FINANCIAL REPORT**

Chairman Wald called on Ms. Tamara Barber, Director of Financial Reporting, North Dakota University System, who presented the annual financial report for the North Dakota University System for the

fiscal year ended June 30, 2004. She said an unqualified opinion was issued on the financial statements. She said the annual unduplicated degree credit headcount for the 2003-04 academic year increased by 4.5 percent over the previous academic year. She said campuses continue to experience steady enrollment increases, resulting in increases in tuition and fee revenues. Ms. Barber reviewed the financial statements and notes to financial statements for the North Dakota University System as a whole and for each campus.

### **AUDIT REPORT FROM ETHANOL PRODUCTION COMPANIES**

At the request of Chairman Wald, the Legislative Council staff distributed a copy of the December 31, 2004, audit report for Alchem, Ltd., LLP. Pursuant to NDCC Section 45-10.2-115, 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 report with the Legislative Audit and Fiscal Review Committee. The report was filed with the committee pursuant to this section. According to the audit report, Alchem, Ltd., LLP, incurred a loss for the year ended December 31, 2004, after deducting payments received from the North Dakota ethanol production incentive program. A copy of the information presented is on file in the Legislative Council office.

### **COMMITTEE DISCUSSION AND STAFF DIRECTIVES**

It was moved by Representative Skarphol, seconded by Representative Kelsch, 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:

1. Veterans Home performance audit followup report (February 14, 2005).
2. Job Service North Dakota (June 30, 2004 and 2003).
3. Workforce Safety and Insurance (June 30, 2004 and 2003).
4. Public Employees Retirement System (June 30, 2004 and 2003).
5. Bank of North Dakota (December 31, 2004 and 2003).
6. Bank of North Dakota information system procedures (December 31, 2004).
7. Municipal Bond Bank (December 31, 2004 and 2003).
8. State Fair Association (September 30, 2004 and 2003).
9. Retirement and Investment Office (June 30, 2004 and 2003).
10. Housing Finance Agency (June 30, 2004 and 2003).

11. Board of University and School Lands (June 30, 2004 and 2003).
12. North Dakota Stockmen's Association (December 31, 2004 and 2003).
13. North Dakota lottery (June 30, 2004).
14. Game and Fish Department (June 30, 2004 and 2003).
15. Department of Veterans Affairs (June 30, 2004 and 2003).
16. Seed Department (June 30, 2004 and 2003).
17. Attorney General (June 30, 2004 and 2003).
18. Information Technology Department (June 30, 2004 and 2003).
19. University System office (June 30, 2004 and 2003).
20. Highway Patrol (June 30, 2004 and 2003).
21. Secretary of State (June 30, 2004 and 2003).
22. Department of Financial Institutions (June 30, 2004 and 2003).
23. Securities Department (June 30, 2004 and 2003).
24. Adjutant General (June 30, 2004 and 2003).
25. State Historical Society (June 30, 2004 and 2003).
26. Protection and Advocacy Project (June 30, 2004 and 2003).
27. Indian Affairs Commission (June 30, 2004 and 2003).
28. ConnectND - Human resource management system information system audit (December 31, 2004).
29. North Dakota Comprehensive Annual Financial Report (June 30, 2004).
30. Statewide single audit report (June 30, 2004 and 2003).
31. Reports available but not selected for presentation:
  - a. Beef Commission (June 30, 2004).
  - b. Dairy Promotion Commission (June 30, 2004 and 2003).
  - c. Dry Pea and Lentil Council (June 30, 2004 and 2003).
  - d. Milk Marketing Board (June 30, 2004 and 2003).
  - e. Oilseed Council (June 30, 2004 and 2003).
  - f. Beginning farmer revolving loan fund (December 31, 2004 and 2003).
  - g. Community water facility loan fund (December 31, 2004 and 2003).
  - h. Development Fund, Inc. (June 30, 2004 and 2003).
  - i. Developmentally disabled facility loan (December 31, 2004 and 2003).

- j. **Guaranteed student loan program (September 30, 2004 and 2003).**
- k. **Board of Nursing (June 30, 2004).**
- l. **Student loan trust (June 30, 2004 and 2003).**
- m. **Board of Chiropractic Examiners (December 31, 2004).**
- n. **Board of Dietetic Practice (September 30, 2003 and 2002).**
- o. **Education Standards and Practices Board (June 30, 2003 and 2002).**
- p. **Board of Optometry (June 30, 2004 and 2003).**
- q. **Board of Pharmacy (June 30, 2004 and 2003).**
- r. **Examining Committee for Physical Therapists (June 30, 2002 and 2001).**
- s. **Examining Committee for Physical Therapists (June 30, 2004 and 2003).**
- t. **Board of Psychologist Examiners (June 30, 2003 and 2002).**
- u. **Board of Accountancy (June 30, 2004).**
- v. **Board of Water Well Contractors (June 30, 2004 and 2003).**

Representatives Wald, Aarsvold, Boucher, Kelsch, Monson, Pollert, Skarphol, Thoreson, and Timm and Senators Bowman, Christmann, Klein, and Lee voted "aye." No negative votes were cast.

Chairman Wald said he asked Ms. Aasen to provide suggested changes to the 12 audit guidelines during the next meeting. He encouraged the committee members to also review the guidelines. He said Brady, Martz & Associates, P.C., Certified Public Accountants, will also be asked to comment on the 12 audit guidelines. The legislative budget analyst and auditor said the responses from the auditors and background information on the 12 audit guidelines will

be sent to committee members prior to the next meeting.

Chairman Wald said representatives of several agencies will be asked to appear before the committee during the next meeting to provide information on their statutory authority for continuing appropriation authority; justification for continuing the authority; and related expenditures, revenues, and fund balance for the 2003-05 biennium and projections for the 2005-07 biennium. He said the agencies will be selected from the continuing appropriation summary report compiled by the Office of Management and Budget.

Representative Skarphol said the continuing appropriation summary report indicated that several of the Workforce Safety and Insurance funds had a negative balance and it would be interesting to get an explanation from the agency. The legislative budget analyst and auditor said the agencies will be asked to provide detailed information on fund balances, including the sources and uses of funds, the reasons for any negative balances, and the corrective action to address the negative balances.

The meeting was adjourned subject to the call of the chair at 4:08 p.m.

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Donald J. Wolf  
Senior Fiscal Analyst

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Jim W. Smith  
Legislative Budget Analyst and Auditor

[ATTACH:1](#)