

NORTH DAKOTA LEGISLATIVE COUNCIL

Minutes of the

LEGISLATIVE AUDIT AND FISCAL REVIEW COMMITTEE

Wednesday, November 29, 2006
Roughrider Room, State Capitol
Bismarck, North Dakota

Representative Francis J. Wald, Chairman, called the meeting to order at 9:00 a.m.

Members present: Representatives Francis J. Wald, Ole Aarsvold, Merle Boucher, Jeff Delzer, RaeAnn G. Kelsch, David Monson, Chet Pollert, Bob Skarphol; Senators Bill L. Bowman, Randel Christmann, Jerry Klein, Judy Lee, Tim Mathern

Members absent: Representatives Andrew G. Maragos, Earl Rennerfeldt, Blair Thoreson, Mike Timm

Others present: See Appendix A

Senator Aaron Krauter, member of the Legislative Council, was also in attendance.

WORKFORCE SAFETY AND INSURANCE PERFORMANCE AUDIT

Chairman Wald called on Mr. Gordy Smith, State Auditor's office, who presented the performance audit report of Workforce Safety and Insurance as of October 26, 2006. Mr. G. Smith said the audit period for which information was collected and reviewed was July 1, 2003, through March 31, 2006. He said the goals of the performance audit were:

1. Has Workforce Safety and Insurance established an adequate procurement system.
2. Has Workforce Safety and Insurance established an adequate human resource management system.
3. Are adequate policies and procedures established to provide appropriate leadership and accountability for Workforce Safety and Insurance.

Mr. G. Smith said from the very start of this performance audit, it was evident to the State Auditor's office that the board and executive management of Workforce Safety and Insurance were against a performance audit being conducted. He said the State Auditor's office remained independent in conducting the performance audit.

Mr. G. Smith said the performance audit report contains 60 recommendations. A copy of the audit recommendations is attached as Appendix B. Based on the performance audit, he said, the State Auditor's office determined:

- Workforce Safety and Insurance does not have an adequate procurement system. Workforce Safety and Insurance has not established sufficient controls necessary to have an adequate procurement system. One area of

concern relates to executive management apparently circumventing controls which have been established. The State Auditor's office noted a significant lack of adequate policies and implementation of policies that have been established.

- Workforce Safety and Insurance has not established an adequate human resource management system. The State Auditor's office noted a number of areas of concern related to aspects of human resources, including hiring of employees, evaluating employees, conducting investigations involving employees, using a pay-for-performance system, making payments to employees, and establishing adequate policies. Due to the lack of an adequate system, the State Auditor's office noted inconsistencies, inappropriate actions being taken, and apparent preferential treatment taking place.
- Workforce Safety and Insurance management has not established adequate policies and procedures to provide appropriate leadership and accountability for the organization. The State Auditor's office noted a number of areas of concern relating to the organization's personnel system, procurement system, strategic planning, and actions, or lack of actions, taken by the executive director.
- The Workforce Safety and Insurance Board has not established adequate policies and procedures to provide appropriate leadership and accountability for the organization. The State Auditor's office noted a number of areas where improvement could be made relating to the board's governance of the organization as well as compliance with its adopted governance model.

Mr. G. Smith said the State Auditor's office reviewed 53 contracts to determine if Workforce Safety and Insurance complied with state procurement laws, administrative rules, Office of Management and Budget policies, and Workforce Safety and Insurance policies and procedures. He said of the 53 contracts reviewed, 6 contracts were not approved by the agency's legal staff as required by Workforce Safety and Insurance policy. He said of the 53 contracts reviewed, 26 contracts did not use the required Attorney General's office's sample

contract per Office of Management and Budget guidelines. He said of the 53 contracts reviewed, 30 contracts did not contain or contained inadequate insurance documentation. He said 35 of the 53 contracts reviewed did not have service requisitions and 21 did not have service evaluations as required by Workforce Safety and Insurance's policies.

Mr. G. Smith said Workforce Safety and Insurance uses a pay-for-performance system which relies on a performance appraisal process. He said Workforce Safety and Insurance's pay-for-performance system has not operated effectively due to problems with the performance appraisal process. He said Workforce Safety and Insurance needs to ensure the performance appraisal process is adequately monitored for compliance with policies and that criteria be established for measuring performance at the beginning of an appraisal period.

Mr. G. Smith said the State Auditor's office noted Workforce Safety and Insurance employees had not received the general salary increases approved by the Legislative Assembly for the 2005-07 biennium. He said a formal Attorney General's opinion was requested and the opinion noted Workforce Safety and Insurance was required to comply with legislative intent to provide the across-the-board annual increases of 4 percent. He said Workforce Safety and Insurance's first attempt at implementing the Attorney General's opinion was inconsistent with legislative intent. He said the State Auditor's office noted Workforce Safety and Insurance used the employee's average fiscal year 2005 salary as a starting point for applying the salary increase. He said using the average salary resulted in employees being paid less than what was required. He said Workforce Safety and Insurance's explanation for using the average fiscal year 2005 salary was that it was trying to convert employee salaries to match the state's system where pay raises are effective on July 1 of each year.

Mr. G. Smith said throughout this audit, indications of low employee morale, problems with communication, and employees fearing retaliation were noted. He said while the performance audit did not specifically include a cultural assessment or morale evaluation, evidence indicated problems existed in these areas. He said a significant number of employees identified favoritism as an issue within the organization.

Mr. G. Smith said the State Auditor's office conducted an employee survey in February 2006 as part of the performance audit. He said of the 192 employees responding to the statement "I am able to take issues to or can disagree with senior management without fear of consequences," 44 percent selected "Strongly Disagree" or "Disagree." He said in review of written comments submitted by employees, 42 employees were identified as making comments related to fear of retaliation, afraid to speak out, and Workforce Safety and Insurance not having an actual open door policy.

In February 2006, Mr. G. Smith said Workforce Safety and Insurance employees were e-mailed information regarding the salaries of employees within the organization. He said after the event, the executive director e-mailed all employees that the "spamming" will be investigated "with every resource we have." He said the executive director identified the Special Investigations Unit, information systems units, general counsel, and himself as the resources used to investigate the "spamming." He said the executive director specifically requested the Special Investigations Unit to conduct an investigation in order to find out who sent the information and whether or not a law was broken. Mr. G. Smith said use of the Special Investigations Unit to attempt to "track down" the individual who e-mailed public information to the employees of Workforce Safety and Insurance violated legislative intent as this unit was not established for such purpose.

Mr. G. Smith said when the executive director made the request to the Special Investigations Unit to conduct the investigation, he provided two names of former employees to include as suspects. He said the Special Investigations Unit accessed the Department of Transportation's driver's license image program. He said the Special Investigations Unit printed at least one of the suspect's pictures from the driver's license image program. He said the Special Investigations Unit showed pictures of the two suspects to employees at the public library where the e-mail had originated. He said the use of the driver's license system to access photos was inappropriate and violated the contract Workforce Safety and Insurance has with the Department of Transportation, which provides that the driver's license image program be used only for official purposes.

Mr. G. Smith said pursuant to North Dakota Century Code (NDCC) Section 65-02-03.1, the Workforce Safety and Insurance Board of Directors is comprised of 11 members--6 representing employers, 3 representing employees, 1 representing medical providers, and 1 appointed at large. He said state law requires one employee member to have received Workforce Safety and Insurance benefits and another employee member to represent organized labor, the board has allowed one member to serve both of these requirements. He said the State Auditor's office requested an Attorney General's opinion to clarify member representation and the formal opinion states one person may not serve as the employee representative who has received Workforce Safety and Insurance benefits and also be the employee representative for organized labor.

Mr. G. Smith said the overall performance of Workforce Safety and Insurance has improved in recent years. He said credit for the turnaround belongs to many, not just current management.

In response to a question from Representative Aarsvold, Mr. G. Smith said procurement contracts were tested according to sampling guidelines and are statistically valid.

In response to a question from Representative Boucher, Mr. G. Smith said a private certified public accounting firm conducts the financial audit of Workforce Safety and Insurance. He said he was unsure whether tests of procurement practices have been conducted as part of previous financial audits. He said audit reports prepared by private certified public accounting firms typically do not include as many audit findings as audit reports prepared by the State Auditor's office.

In response to a question from Representative Wald, Mr. G. Smith said the State Auditor's office did not identify any instances of missing materials, equipment, or supplies.

In response to a question from Senator Mathern, Mr. G. Smith said the state procurement regulations were established to ensure that products are obtained at the most reasonable price and to ensure fairness among vendors competing for business.

In response to a question from Representative Boucher, Mr. G. Smith said internal controls are necessary to minimize the risk that fraud may occur. He said auditors cannot guarantee that all fraud will be detected during the audit process. He said Workforce Safety and Insurance's failure to follow internal controls relating to procurement practices increases the risk of fraud; however, it does not mean that fraud occurred.

In response to a question from Representative Boucher, Mr. G. Smith said the performance audit report contains a finding that Workforce Safety and Insurance selected individuals for employment who did not meet the minimum qualifications for the position. He said this practice occurred throughout the agency and for all position "levels."

In response to a question from Senator Klein, Mr. G. Smith said Workforce Safety and Insurance is responsible for establishing the necessary qualifications for each position.

In response to a question from Representative Skarphol, Mr. G. Smith said the Legislative Assembly appropriates a single amount to Workforce Safety and Insurance for necessary operations of the agency. He said this single line appropriation gives Workforce Safety and Insurance more flexibility than most other state agencies to increase salary ranges.

Senator Mathern said he received a letter from a former Workforce Safety and Insurance employee who indicated that the high turnover rate at the department is due to a "deteriorating" work environment. He said the former employee indicated that there is constant abuse of workers, threats, harassment, and a total lack of leadership at Workforce Safety and Insurance.

Representative Wald said some employees are resistant to change. He said Workforce Safety and Insurance has acknowledged that there is a turnover and morale problem and will work to address this issue.

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

will conduct a followup review of Workforce Safety and Insurance within the next 18 to 24 months. He said as part of the followup review, the State Auditor's office will survey employees to determine if the work environment within Workforce Safety and Insurance has improved.

Representative Boucher asked Workforce Safety and Insurance to provide the Legislative Assembly or the members of the Legislative Audit and Fiscal Review Committee with periodic updates regarding the progress of implementing the performance audit recommendations.

Senator Lee said it is the responsibility of the Workforce Safety and Insurance Board to implement the performance audit recommendations.

In response to a question from Representative Boucher, Mr. G. Smith said the executive director of Workforce Safety and Insurance provided salary increases to seven of his eight "direct reports" which exceeded the compensation plan computed by Workforce Safety and Insurance. He said the compensation plan was based on a review performed by the Hay Group, which is an independent consultant.

In response to a question from Representative Boucher, Mr. Charles Blunt, Executive Director and CEO, Workforce Safety and Insurance, said he would provide the committee with information identifying the seven "direct reports," including their salaries, responsibilities, and prior employment history.

Chairman Wald called on Mr. Bob Indvik, Chairman, Workforce Safety and Insurance Board, who said NDCC Section 65-02-03.3 provides the powers and duties of the Workforce Safety and Insurance Board. He said the board has complied with this section of law. He said the board has adopted the "Carver Policy Governance Model." He said this is a model of governance designed to enable a board to focus on the larger areas, to delegate with clarity, to control management's job without meddling, and to rigorously evaluate the accomplishment of the organization. He said Mr. John Carver has been invited to review the board's governance policy.

Mr. Indvik said he does not agree with the audit recommendation that the daily compensation rate for the members of the Workforce Safety and Insurance Board is not adequate. He said the board members serve because of civic responsibility and not because of the rate of compensation.

Mr. Indvik said employee morale fluctuates and is difficult to judge. He said the pay-for-performance system established by Workforce Safety and Insurance has created some hard feelings among certain employees.

In response to a question from Representative Boucher, Mr. Indvik said the Workforce Safety and Insurance Board intends to implement the audit recommendations.

In response to a question from Representative Boucher, Mr. Indvik said according to the performance audit report, the Workforce Safety and Insurance

Board meets every three months for, on average, three hours per meeting. However, he said, this does not include the time spent by board members in subcommittee meetings. He said the governance model followed by the board provides for the majority of the board's work to be completed by subcommittees.

In response to a question from Representative Skarphol, Mr. Indvik said the Workforce Safety and Insurance Board has developed performance goals. He said the board directed the executive director to establish a plan to achieve those goals and related measurements. He said Workforce Safety and Insurance would provide committee members with a copy of the goals and measurements.

In response to a question from Senator Bowman, Mr. Indvik said the board receives legal assistance from both staff attorneys and the Attorney General's office. He said legal counsel is in attendance during each board meeting. Representative Skarphol said the board membership should include an attorney and an individual with a background in information technology.

Representative Kelsch said the Workforce Safety and Insurance Board receives a daily compensation rate of \$100 for each meeting attended or for other board-related duties. She said pay can be an incentive for businessmen and employees to serve on a board. Mr. Indvik said the board relies heavily on consultants with industry expertise to make business decisions.

Chairman Wald called on Mr. Blunt to comment on the performance audit. A copy of the information presented is on file in the Legislative Council office. Mr. Blunt said the narrative included in the performance audit is very "negative." He said things are not as bad at Workforce Safety and Insurance as detailed in the performance audit report. He said Workforce Safety and Insurance has great employees who do a difficult job. He said Workforce Safety and Insurance will implement the performance audit recommendations.

In response to a question from Representative Boucher, Mr. Blunt said one of three internal auditor positions within Workforce Safety and Insurance was replaced with a new leadership and organization excellence executive position. He said the third internal auditor position had been created only for a short period of time. He said it was determined that there was not enough work for three internal auditors.

In response to a question from Representative Wald, Mr. Blunt said the performance audit, performance review, and financial audit of Workforce Safety and Insurance were being conducted simultaneously. He said in addition to performing their regular duties, employees spent a significant amount of time assisting auditors. He said Workforce Safety and Insurance has also recently implemented a new computer system and strategic plan. He said these additional responsibilities and changes have

increased stress levels and affected employee morale.

In response to a question from Senator Christmann, Mr. Blunt said he believes tactics used by the State Auditor's office during the performance audit were aggressive and unprofessional.

Senator Mathern said it is difficult to raise issues that may improve the department if they are taken as a personal attack.

Senator Lee said it is common for any business to have communication problems among employees. She said Workforce Safety and Insurance should focus on the issues identified within the performance audit that can be corrected and improved.

In response to a question from Representative Skarphol, Mr. Blunt said if he had to choose he would say the performance audit was more critical than constructive.

Chairman Wald called on Mr. Dick Johnson, former Workforce Safety and Insurance Board member, Bismarck, who commented on the performance audit report. Mr. Johnson said Workforce Safety and Insurance is successfully completing its duties and responsibilities.

Chairman Wald called on Mr. Chuck Peterson, former Chairman of the Workforce Safety and Insurance Board, Bismarck, who commented on the performance audit. Mr. Peterson said added pressure placed on both management and staff to improve performance can create stress and morale problems.

Chairman Wald called on Mr. David L. Kemnitz, Chairman, North Dakota AFL-CIO, Bismarck, who commented on the performance audit report. Mr. Kemnitz said according to the performance audit report, the oversight of Workforce Safety and Insurance needs to improve. He said there needs to be changes to the membership of the Workforce Safety and Insurance Board, including providing a more even balance of employees, as compared to employers, serving on the board.

Chairman Wald called on Mr. Sebald Vetter, President, Concerned Advocate Rights for Injured Workers, Bismarck, who commented on the performance audit report. He said management of Workforce Safety and Insurance should be held responsible for violations of law that may have been committed.

The committee recessed for lunch at 12:15 p.m. and reconvened at 1:00 p.m.

Chairman Wald called on Representative George J. Keiser who commented on the Legislative Council's 2005-06 interim Workers' Compensation Review Committee. He said the committee received testimony from injured workers regarding their workers' compensation claims and whether changes should be made to workers' compensation laws. As a result of the testimony received, he said, the committee has introduced bills that would change five sections of the North Dakota Century Code relating to workers' compensation laws. He said the injured

workers who testified were not involved in "active" cases.

WORKFORCE SAFETY AND INSURANCE PERFORMANCE REVIEW

Chairman Wald called on Mr. Malcolm Dodge, Octagon Risk Services, Inc., Oakland, California, who presented the performance review report for Workforce Safety and Insurance for the years ended December 31, 2005 and 2004. Mr. Dodge said the audit review focuses on the following eight elements that were felt to be the highest priorities for Workforce Safety and Insurance:

1. Assess Workforce Safety and Insurance's performance measurements in keeping with NDCC Section 65-02-30.
2. Evaluate Workforce Safety and Insurance's loss prevention programs.
3. Assess whether Workforce Safety and Insurance's information technology team is being managed in an effective, cost-efficient manner.
4. Determine if the Workforce Safety and Insurance Board is operating in accordance with NDCC Sections 65-02-03.1 and 65-02-03.3 and within the board's bylaws.
5. Evaluate the effectiveness of expenditures incurred by Workforce Safety and Insurance's fraud unit in accordance with NDCC Section 65-02-23.
6. Evaluate the bill review and utilization review services provided by Workforce Safety and Insurance.
7. Review the policyholder services collections function, the premium audit function, the premium billing process, the overall effectiveness of Workforce Safety and Insurance's experience rating plan and the existing rate classification manual.
8. Review prior recommendations.

Mr. Dodge said the review includes 109 recommendations by element and priority as follows:

Element	High Priority	Medium Priority	Low Priority	Total
One	5	6	4	15
Two	2	7	1	10
Three	20	9	6	35
Four	5	3	1	9
Five	1	0	1	2
Six	8	7	0	15
Seven	3	14	6	23
Eight	0	0	0	0
Total	44	46	19	109

Mr. Dodge said key observations from the performance review include:

1. Workforce Safety and Insurance performance measures:
 - a. Legal defense costs need to be measured over a broader span of time to

demonstrate whether Workforce Safety and Insurance is successfully controlling these costs.

- b. The customer satisfaction survey should be expanded to include a wider array of claim types, including individuals whose claims were denied.
2. Safety and loss prevention programs:
 - a. Workforce Safety and Insurance should assess the results of its new safety outreach and risk management programs when data is sufficiently aged to measure outcomes.
 - b. The loss prevention staff would benefit from ongoing professional development, including seeking certification in their chosen specialty. Upon completing certification, these employees may be rewarded with a higher compensation package.
3. Information technology:
 - a. Communication needs to be consistently better within the department and philosophical disagreements cannot be allowed to impact the department's overall performance.
 - b. Formal project management should exist for all information technology projects.
 - c. Information technology staff should be available at least during the same hours as the customers they support.
 - d. Workforce Safety and Insurance should complete its data integrity project to upgrade all currently "mediocre" or "bad" data to "good" data.
4. Workforce Safety and Insurance Board:
 - a. The board should seek clarification of legislative intent regarding whether there is a timeframe requirement for when the injured employee member received Workforce Safety and Insurance benefits. The employee member currently serving on the board received workers' compensation benefits many years ago.
5. Fraud:
 - a. The principal areas of weakness that remain for the Special Investigations Unit is medical provider fraud. Workforce Safety and Insurance may need to consider external training resources to successfully implement effective medical provider fraud programs.
6. Medical services:
 - a. A training manual is needed for bill reviewers.
 - b. In the latter part of 2005 and into early 2006, Workforce Safety and Insurance experienced a major growth in its backlog of medical bills. This backlog was resolved through an autoadjudication

process that could have been better devised.

7. Policyholder services:
 - a. To help ensure that employers keep workers' compensation safety at the forefront of their decisionmaking, the experience modification cap should be eliminated.
 - b. Annual and five-year rotational plans are needed to audit employers.

Mr. Dodge said based on a review of prior recommendations, it was determined that 20 recommendations were determined to be fully implemented, 28 were partially implemented, 8 were not implemented, and 3 recommendations are no longer applicable.

In response to a question from Representative Wald, Mr. Dodge said Octagon Risk Services, Inc., works with both private and public sector businesses.

In response to a question from Representative Boucher, Mr. Dodge said Octagon Risk Services, Inc., has participated in four performance reviews of Workforce Safety and Insurance--two as a subcontractor and two as the lead contractor. He said certain departments within Workforce Safety and Insurance have done a better job than other departments in implementing prior recommendations.

In response to a question from Representative Skarphol, Mr. Dodge said Workforce Safety and Insurance needs to spend more money on training employees on how to identify medical provider fraud. Mr. Blunt said provider fraud is very difficult to prove and requires a significant amount of evidence.

In response to a question from Representative Skarphol, Mr. Dodge said the original bid for the performance review of Workforce Safety and Insurance provided for 11 elements. He said three of these elements (procurement system, human resources, and leadership and accountability) were included in the performance audit conducted by the State Auditor's office. He said the additional consulting fee for these three elements would have been \$75,000.

In response to a question from Senator Bowman, Mr. Dodge said generally the performance recommendations should be implemented within 6 to 12 months.

In response to a question from Representative Skarphol, Mr. Dodge said it is important for Workforce Safety and Insurance to partner with the Information Technology Department for security issues. He said the best way to maximize information technology resources is to have the best tools and people capable of utilizing the tools.

In response to a question from Representative Boucher, Mr. Dodge said the board seems to rely significantly on the knowledge base of the executive director. He said it is important to have board members who understand how to run a business.

In response to a question from Representative Wald, the legislative budget analyst and auditor said

compensation for board members is provided in related statute for each state board. He said there is no established uniform rate of compensation for board members.

Chairman Wald called on Mr. Blunt who provided information on the performance review. A copy of the information presented is on file in the Legislative Council office. Mr. Blunt said of the 109 submitted performance review recommendations, Workforce Safety and Insurance concurs with 81 percent, partially concurs with 10 percent, and does not concur with 9 percent. He said Workforce Safety and Insurance and its board would like to thank Octagon Risk Services, Inc., for all its work on this performance review.

In response to a question from Representative Wald, Workforce Safety and Insurance provided information regarding the 14 new employees it has requested for the 2007-09 biennium. A copy of the information is attached as Appendix C.

STATE AGENCY AND INSTITUTION AUDIT REPORTS

Chairman Wald called on Mr. Ed Nagel, State Auditor's office, who presented the audit report for the State Water Commission for the years ended June 30, 2005 and 2004. Mr. Nagel reviewed the auditor's responses to the committee's guidelines and said the report contains two findings of internal control weaknesses relating to PeopleSoft access controls and misstated accounts in the financial statements. He said the Office of Management and Budget is responsible for these security roles. He said the Office of Management and Budget has corrected this internal control weakness so no recommendation will be made to the State Water Commission. He said the State Auditor's office found and corrected material misstatements to accounts within the State Water Commission's financial statements.

Mr. Nagel presented the audit report for the Department of Agriculture for the years ended June 30, 2005 and 2004. He reviewed the auditor's responses to the committee's guidelines and said the report does not contain any findings or recommendations.

In response to a question from Representative Skarphol, Ms. Lynette Baumiller, Department of Agriculture, said total transfers for the Department of Agriculture were significantly less in fiscal year 2005 as compared to fiscal year 2004 due to timing differences. She said licenses, permits, and fee revenues were also less in fiscal year 2005 as compared to fiscal year 2004 due to biennial fees being collected during the first year of the biennium.

Mr. Nagel presented the audit report for the Department of Commerce for the years ended June 30, 2005 and 2004. He reviewed the auditor's responses to the committee's guidelines and said the report contains two internal control findings relating to

weaknesses in the receipting process and inventory procedures.

Mr. Nagel said the audit report for the Department of Commerce contains one recommendation for operational improvement relating to establishing a national resources bond application process. He said NDCC Chapter 21-11 allows any privately or cooperatively owned enterprise to apply for a loan for the purpose of planning, constructing, acquiring, equipping, improving, or extending facilities for the conversion of North Dakota's natural resources into low-cost power, the transmission of such power, and the acquisition of real and personal property and water and mineral rights needed for such facilities. He said the Division of Economic Development and Finance of the Department of Commerce is responsible for establishing the application form, investigating applicants, and evaluating the technical and economic feasibility of the operation plan submitted by applicants. He said the Department of Commerce is to collect an application fee not to exceed \$50,000. If an applicant is approved, the application is filed with the Industrial Commission.

Mr. Nagel said the Division of Economic Development and Finance was not aware of this North Dakota Century Code section and, therefore, has not developed an application process for companies interested in applying for this loan. He said the department is unaware of any company having expressed interest in obtaining such a loan.

In response to a question from Representative Skarphol, the Department of Commerce provided information regarding the department's 2003-05 biennium total federal and special funds expenditures. According to the Department of Commerce, total federal and special funds expenditures were approximately \$11.8 million less than the amount appropriated primarily due to a reduction in federal funds received by the department. Most federal programs within the Division of Community Services received less federal funds than were anticipated, including the energy program, the HOME program, and the community services block grant.

Mr. Nagel presented the audit report for the Department of Career and Technical Education for the years ended June 30, 2005 and 2004. He reviewed the auditor's responses to the committee's guidelines and said the report contains a recommendation for operational improvement relating to implementing efficiencies in purchasing card procedures.

Mr. Paul Welk, State Auditor's office, presented the audit report for the State Treasurer for the years ended June 30, 2005 and 2004. He reviewed the auditor's responses to the committee's guidelines and said the report contains three internal control findings relating to reclassifying the controller position to an accounting manager or accounting/budget specialist II or III classification, reconciling the state's cash balance on PeopleSoft to the Bank of North Dakota, computer access control weaknesses, and PeopleSoft access control weaknesses. He said the report

contains three findings of noncompliance with legislative intent relating to incorrect monthly distributions of coal severance taxes, incorrect monthly distributions of oil and gas production taxes, and funds being deposited into incorrect accounts. He said three prior audit recommendations were not implemented. He said these prior audit recommendations relate to reclassifying the controller position, incorrect distributions of coal severance taxes, and incorrect calculations of the per capita limitation on oil and gas production taxes for the city of Medora.

In response to a question from Representative Delzer, Mr. Welk said improper daily enrollment information was submitted by school superintendents which resulted in the incorrect coal severance tax distributions.

Chairman Wald called on Ms. Kelly Schmidt, State Treasurer, who said the State Auditor's office has changed procedures relating to the collection of daily enrollment figures from school districts to avoid further errors. She said the oil and gas production system has been updated to correctly distribute the total amount available to the remaining cities within the affected county when there is dissolution of a city.

In response to a question from Representative Skarphol, the Legislative Council staff determined that pursuant to NDCC Section 15.1-27-25, the minerals management tax relates to federal funds received by the state for the purpose of promoting the mining of coal, phosphate, oil, oil shale, gas, and sodium under public domain. These funds must be credited to the state general fund. The State Treasurer is to allocate 50 percent of the funding to the counties in which the minerals were produced based on the proportion each county's mineral royalty revenue bears to the total amount of mineral royalty received by the state. The counties may use the money received for the planning, construction, and maintenance of public facilities and the provision of public services. The remaining federal funding is to be distributed as state aid to school districts.

Mr. Nagel presented the audit report for the Mill and Elevator for the years ended June 30, 2006 and 2005. He reviewed the auditor's responses to the committee's guidelines and said the report does not contain any findings or recommendations.

In response to a question from Representative Wald, Mr. Vance Taylor, General Manager, Mill and Elevator Association, said the Mill and Elevator transferred \$200,000 to the Department of Commerce during fiscal year ended June 30, 2006, for the North Dakota Trade Office.

Chairman Wald called on Mr. Darrell Lingle, Eide Bailly LLP, Certified Public Accountants, who presented the audit report for Workforce Safety and Insurance for the years ended June 30, 2006 and 2005. He reviewed the auditor's responses to the committee's guidelines and said the audit report contains an unqualified opinion and contains two internal control findings. He said Workforce Safety

and Insurance should continue to improve the case reserving process through education of analysts and providing the tools necessary to bring consistency to the reserving process. He said the claims management system could potentially malfunction and establish an "end date" for a reserve liability that is still in force. He said Workforce Safety and Insurance should rectify data integrity issues with the case management system to ensure that the data is complete and accurate.

Mr. Tony Hauck, Eide Bailly LLP, Certified Public Accountants, presented the audit report for Job Service North Dakota for the years ended June 30, 2006 and 2005. He reviewed the auditor's responses to the committee's guidelines and said the audit report contains an unqualified opinion and does not contain any findings or recommendations.

Mr. Hauck presented the audit report for the State Fair Association for the years ended September 30, 2006 and 2005. He reviewed the auditor's responses to the committee's guidelines and said the audit report contains an unqualified opinion. He said the report contains one internal control finding relating to segregation of accounting duties and one finding of noncompliance with legislative intent relating to failure to complete a physical inventory during fiscal year 2006.

In response to a question from Representative Monson, Mr. Hauck said there are two accounting positions within the State Fair Association. He said proper segregation of accounting duties usually requires a minimum of four accounting positions.

CONNECTND STUDENT ADMINISTRATION COMPONENT INFORMATION TECHNOLOGY AUDIT

Chairman Wald called on Mr. Donald LaFleur, State Auditor's office, who presented the information technology audit report of the student administration component of the ConnectND system. He said ConnectND student administration is considered a "high-risk" information system because it is a relatively new system and is used by North Dakota University System institutions to maintain student information. He said ConnectND student administration is a comprehensive web-based student information system. He said it records information, such as student records, financial aid, and financial information. He said it is utilized throughout the student's academic career from recruiting to graduation.

Mr. LaFleur said the audit report includes the following recommendations for the North Dakota University System:

1. Design roles to ensure access to Social Security numbers is properly restricted.
2. Require passwords be changed for nonstudent accounts every 60 to 90 days.
3. Secure necessary screens so information is restricted to a user's institution.

4. Perform a regular review of default accounts to ensure they are locked.
5. Perform a regular review of superuser accounts to determine if they are necessary.
6. Develop a formal policy to ensure credit card numbers are not stored in ConnectND student administration.
7. Implement a reliable process to ensure the accounting line table reconciles between ConnectND student administration and ConnectND finance.
8. Implement controls to prevent backdating of effective dates on the item general ledger interface table.
9. Strengthen controls to prevent backdating the effective date when a class is dropped.
10. Develop a formal contingency plan for ConnectND student administration.
11. Develop comprehensive documentation outlining policies and procedures to be used by all universities, which at a minimum address proper internal controls and compliance with state law and North Dakota University System policy.

In response to a question from Representative Delzer, Mr. LaFleur said backdating of the effective date when a class is dropped accounted for a very small number of students.

In response to a question from Senator Christmann, Ms. Laura Glatt, Vice Chancellor of Administrative Affairs, North Dakota University System, said there are legitimate instances where a record may be backdated to reflect a "No Record Drop," including cases where a student petition is approved by a campus committee or a student preregisters as an undergraduate and then is accepted as a graduate student. Representative Skarphol said the North Dakota University System should be very "judicious" in allowing backdating of the effective date of dropped classes.

INFORMATION TECHNOLOGY DEPARTMENT - ANNUAL REPORT

Chairman Wald called on Mr. Mike Ressler, Deputy Chief Information Officer, Information Technology Department, who distributed a copy of the department's annual report on information technology projects, services, and performance measures, pursuant to NDCC Section 54-59-19. A copy of the report is on file in the Legislative Council office. Mr. Ressler said total revenue for the Information Technology Department in fiscal year 2006 was \$37.7 million. He said 10 agencies generated 66 percent of the revenue. He said software development generated 21 percent of the revenue. He said a second data center was created in Mandan to provide disaster recovery services previously acquired through IBM in Boulder, Colorado. He said the relocation of the data center allows the department to bring critical systems up within eight

hours in case of a disaster at the Bismarck data center.

In response to a question from Senator Bowman, Mr. Ressler said overall information technology costs for state government will probably not "go down" in the future. He said it is important for state government to show the "value" received from technology.

In response to a question from Representative Delzer, Mr. Ressler said state agencies are required to provide a business case for each information technology project undertaken.

In response to a question from Representative Wald, Mr. Ressler said the employee growth rate within the Information Technology Department is primarily due to the increase in the number of application projects to be implemented by state agencies.

Representative Kelsch said technology has become less expensive; however, there is more technology used today than in the past.

COMMITTEE DISCUSSION AND STAFF DIRECTIVES

Senator Mathern asked that the Potato Council audit report be presented during the next meeting of the Legislative Audit and Fiscal Review Committee. Representative Skarphol asked that the Wheat Commission audit report be presented during the next meeting.

It was moved by Representative Kelsch, seconded by Senator Mathern, 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. **Workforce Safety and Insurance performance audit (October 26, 2006).**
2. **Workforce Safety and Insurance performance review (December 31, 2005 and 2004).**
3. **State Water Commission (June 30, 2005 and 2004).**
4. **Department of Agriculture (June 30, 2005 and 2004).**
5. **Department of Commerce (June 30, 2005 and 2004).**
6. **Department of Career and Technical Education (June 30, 2005 and 2004).**
7. **State Treasurer (June 30, 2005 and 2004).**
8. **Mill and Elevator Association (June 30, 2006 and 2005).**
9. **Workforce Safety and Insurance (June 30, 2006 and 2005).**
10. **Job Service North Dakota (June 30, 2006 and 2005).**
11. **State Fair Association (September 30, 2006 and 2005).**
12. **Student administration component of the ConnectND system information technology audit (June 30, 2006).**

13. Reports available but not selected for presentation:

- a. **Soybean Council (June 30, 2006 and 2005).**
- b. **Dry Bean Council (June 30, 2006 and 2005).**
- c. **Barley Council (June 30, 2006 and 2005).**
- d. **Corn Utilization Council (June 30, 2006 and 2005).**
- e. **Ag PACE fund (June 30, 2006 and 2005).**
- f. **Beef Commission (June 30, 2006 and 2005).**
- g. **Dairy Promotion Commission (June 30, 2006 and 2005).**
- h. **Development Fund, Inc. (June 30, 2006 and 2005).**
- i. **Oilseed Council (June 30, 2006 and 2005).**
- j. **Milk Marketing Board (June 30, 2006 and 2005).**
- k. **Dry Pea and Lentil Council (June 30, 2006 and 2005).**
- l. **Firefighter's Association (April 30, 2006 and 2005).**

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

In response to a question from Representative Wald, Mr. G. Smith said the State Auditor's office has been requested by the Legislative Audit and Fiscal Review Committee to complete the following performance audits:

1. A performance audit of the University of North Dakota School of Medicine and Health Sciences.
2. A performance audit on state agency cell phone usage, including a review of the propriety of state cell phone usage, the types of cell phone plans purchased, the number of minimally used cell phones, and various alternative methods to reimburse state employees for cell phone usage.
3. A performance audit of Fleet Services.

Mr. G. Smith said the State Auditor's office has begun preliminary work on the performance audit of the University of North Dakota School of Medicine and Health Sciences.

Representative Wald said a representative of the Dickinson Research Extension Center indicated concern with high state motor pool rates.

The legislative budget analyst and auditor said the North Dakota University System could be asked to present information during the next meeting of the Legislative Audit and Fiscal Review Committee regarding motor pool rates charged to North Dakota University System institutions and agricultural research and extension centers. He said the Legislative Audit and Fiscal Review Committee has

met in January during the past few sessions to hear the state's Comprehensive Annual Financial Report and the annual financial report for the North Dakota University System.

The meeting was adjourned subject to the call of the chair at 4:55 p.m.

Donald J. Wolf
Senior Fiscal Analyst

Jim W. Smith
Legislative Budget Analyst and Auditor

[ATTACH:3](#)