

NORTH DAKOTA LEGISLATIVE COUNCIL

Minutes of the

LEGISLATIVE AUDIT AND FISCAL REVIEW COMMITTEE

Wednesday, January 21, 1998
Roughrider Room, State Capitol
Bismarck, North Dakota

Representative Mike Timm, Chairman, called the meeting to order at 9:00 a.m.

Members present: Representatives Mike Timm, Ole Aarsvold, Rex R. Byerly, John Dorso, Gereld F. Gerntholz, Richard Kunkel, Andrew G. Maragos, Stacey L. Mickelson, Jim Poolman, Bob Skarphol, Francis J. Wald, Gerry Wilkie; Senators Evan E. Lips, Duane Mutch, Ken Solberg, Dan Wogsland

Member absent: Senator Harvey D. Tallackson

Others present: See Appendix A

It was moved by Representative Wald, seconded by Senator Lips, and carried on a voice vote that the minutes of the previous meeting be approved as mailed.

Mr. John Mongeon, Brady Martz and Associates, Certified Public Accountants, presented the Retirement and Investment Office audit report for the year ended June 30, 1997. He reviewed the auditor's responses to the committee's guidelines and said the report contains one finding and related recommendation relating to reimbursing an employee for moving expenses in excess of the maximum amount allowed. He said the report contains an unqualified opinion.

Mr. Mongeon presented the Public Employees Retirement Board audit report for the year ended June 30, 1997. He reviewed the auditor's responses to the committee's guidelines and said the report contains three findings and related recommendations. He said the first finding relates to the accuracy of documentation maintained in participant files and the deferred compensation data base. He said the second and third findings relate to improving the accuracy of financial information obtained from semiannual provider summaries. Mr. Mongeon said the report contains an unqualified opinion.

Representative Byerly asked if the state is subsidizing the political subdivisions which participate in the Public Employees Retirement System. Mr. Sparb Collins, Public Employees Retirement System, said employees of

participating political subdivisions begin accruing benefits on the date the political subdivision joins the Public Employees Retirement System. He said the fund does not recognize employee service credit prior to the date of the political subdivision joining the Public Employees Retirement System. He said this way the political subdivisions pay their own way and there is no cost subsidization by the state.

Representative Wald asked what the fund earned for the fiscal year ending June 30, 1997. Mr. Scott Engmann, Retirement and Investment Office, said the fund earned 19.48 percent for the fiscal year ending June 30, 1997.

In response to a question from Representative Maragos, Mr. Engmann said the actuarial assumptions used for the Teachers' Fund for Retirement and the Public Employees Retirement System are based on average annual returns of eight percent.

Mr. Ron Johnke, Brady Martz and Associates, Certified Public Accountants, presented the Veterans Home audit report for the year ended June 30, 1997. He reviewed the auditor's responses to the committee's guidelines and said the report contains one finding and related recommendation relating to spending over 75 percent of the salary appropriation within the first 18 months of the biennium. He said the report contains an unqualified opinion.

Mr. Mongeon presented the Job Service North Dakota audit report for the year ended June 30, 1997. He reviewed the auditor's responses to the committee's guidelines and said the report does not contain any findings or recommendations. He said the report contains an unqualified opinion.

Mr. Johnke presented the Mill and Elevator Association audit report for the years ended June 30, 1997 and 1996. He reviewed the auditor's responses to the committee's guidelines and said the report contains two findings and related recommendations. He said the first finding relates to the mill not taking an annual inventory of property in the data processing area and the

second finding relates to the payment of moving expenses in excess of the maximum amount allowed. He said the report contains an unqualified opinion.

In response to a question from Representative Mickelson, Mr. Mike Strobel, Mill and Elevator Association, said there were two instances in which the moving expense limit of \$5,000 was exceeded. He said the first incident was his reimbursement which totaled slightly under \$6,000 and the second was the lab manager which was a total of approximately \$12,000. Mr. Strobel said he paid the Mill and Elevator back for his moving expenses in excess of \$5,000. He said the lab manager's \$12,000 was for both moving expenses and real estate expenses.

It was moved by Representative Byerly, seconded by Representative Skarphol, and carried that the Legislative Audit and Fiscal Review Committee recommend that future financial audit reports of the North Dakota Mill and Elevator Association include information on the amount of bonuses paid to mill employees under any profit-sharing agreements. Voting "aye" were Representatives Timm, Byerly, Gerntholz, Kunkel, Mickelson, Skarphol, and Wald and Senator Solberg. Voting "nay" were Representatives Aarsvold, Maragos, Poolman, and Wilkie and Senators Lips, Mutch, and Wogsland.

It was moved by Representative Maragos, seconded by Representative Wilkie, and carried that the committee accept the following reports:

- **For the year ended June 30, 1997**
Retirement and Investment Office
Public Employees Retirement Board
Veterans Home
Job Service North Dakota
- **For the years ended June 30, 1997 and 1996**
Mill and Elevator Association

It was moved by Senator Solberg, seconded by Representative Skarphol, and failed on a voice vote that the previous motion be amended to not include approval of the Mill and Elevator Association audit report.

Voting "aye" were Representatives Timm, Aarsvold, Byerly, Gerntholz, Kunkel, Maragos, Mickelson, Poolman, Skarphol, Wald, and Wilkie and Senators Lips, Mutch, Solberg, and Wogsland. No negative votes were cast.

Mr. Alton Nitschke, Eide Helmeke PLLP, Certified Public Accountants and Consultants, presented the North Dakota Development Fund, Inc., audit report for the years ended June 30, 1997 and 1996. He reviewed the auditor's responses to the committee's guidelines and said the report contains two findings and related

recommendations. He said the first finding relates to the lack of proper supporting documentation for travel expense reimbursements and the second finding relates to the lack of additional collateral for a certificate of deposit in excess of FDIC coverage. He said the report contains an unqualified opinion.

Mr. Bryan Dvirnak, North Dakota Development Fund, Inc., presented information on the status of the investments held by the fund. A copy of his presentation is on file in the Legislative Council office. He said to date 99 projects have been funded totaling \$19,475,600. He said there are an additional 16 projects totaling \$3,403,726 pending funding. He said if all 16 projects were funded, total funding from the North Dakota Development Fund, Inc., would be \$22,879,326. He said the focus of the fund has switched from taking equity positions to issuing more debt instruments. He said the fund has become more selective on which equity positions it invests in.

Mr. Dvirnak said the fund generates approximately \$3.4 million of earnings per biennium. He said the default rate on investments made by the fund was 32 percent in 1994. He said since that time the rate has dropped to 20.2 percent in 1995, 13 percent in 1996, 9.6 percent in 1997, and was 8.14 percent as of December 31, 1997.

Representative Maragos requested that he be provided a written copy of the fund's strategy regarding the use of put options.

In response to a question from Representative Skarphol, Mr. Dvirnak provided the committee with a list of investments that have been charged off. A copy of the list is on file in the Legislative Council office. Mr. Dvirnak said as of December 31, 1997, the fund has charged off investments totaling \$2,856,700, which \$501,700 was rural fund investments. He said 94.7 percent of the investments charged off were investments made prior to the fund's management changes in 1994.

In response to a question from Representative Byerly, Mr. Dvirnak said he would provide committee members with information on the various types of debt instruments issued by the fund.

In response to a question from Representative Skarphol, Mr. Dvirnak said he would provide committee members with a list of investments that have been fully repaid.

Chairman Timm distributed a memorandum prepared by the Legislative Council entitled *Payment of Moving Expenses for New State Employees*. He said since this topic came up in two of the audit reports presented earlier in the meeting,

the information may be helpful to committee members.

Mr. Nitschke presented the Board of University and School Lands audit report for the years ended June 30, 1997 and 1996. He reviewed the auditor's responses to the committee's guidelines and said the report does not contain any findings or recommendations. He said the report contains an unqualified opinion.

Mr. Nitschke presented the Workers Compensation Bureau audit report for the years ended June 30, 1997 and 1996. He reviewed the auditor's responses to the committee's guidelines and said the report does not contain any findings or recommendations. He said the report contains an unqualified opinion.

Mr. Nitschke presented the Technology Transfer, Inc., audit report for the years ended June 30, 1997 and 1996. He reviewed the auditor's responses to the committee's guidelines and said the report does not contain any findings or recommendations. He said the report contains a going concern opinion due to legislation passed by the 1997 Legislative Assembly which transferred Technology Transfer, Inc., to the North Dakota Development Fund, Inc., on July 1, 1999.

Mr. John Van Middlesworth, Department of Economic Development and Finance, presented information on the status of investments held by Technology Transfer, Inc. He said since the inception of the fund 140 applications totaling approximately \$4.5 million have been approved. He said this funding has leveraged an additional \$16 million of other investments and has helped to create approximately 300 jobs. Mr. Van Middlesworth said to date there has been approximately \$283,000 repaid to the fund and there is approximately \$450,000 available in the fund.

Mr. Van Middlesworth said the applications approved have been in the following categories:

- \$3.3 million of royalty agreements,
- \$500,000 of equity investments,
- \$243,000 of debt instruments, and
- \$327,000 of grants.

Representative Byerly requested that committee members be provided with a consolidated list showing investments made by both the Development Fund and Technology Transfer fund. He asked that the information be provided by company and by type of investment and include all projects funded since the inception of each fund, including the current status of the investment. He asked that the information also show whether the investment has been written off, is still being collected, or has been repaid.

Representative Wald asked about the strategies referred to in the audit report regarding the

continuation of the Technology Transfer fund. Mr. Van Middlesworth said they originally talked to the Governor and there is some concern about the Technology Transfer fund concept being continued. He said nothing has been decided on at this point as how to approach this subject during the next legislative session.

Mr. Kevin Cramer, Department of Economic Development and Finance, said the Technology Transfer fund function will not go away when the fund is merged with the Development Fund. He said the different concept and practice of investing in technology projects is something that needs to be continued after the fund is merged into the Development Fund. He said the concern for the continuation of this concept is not necessarily for the continuation of a separate entity, but for the continued investment into these types of projects.

Mr. Ed Nagel, State Auditor's office, presented the Potato Council audit report for the two years ended June 30, 1996. He reviewed the auditor's responses to the committee's guidelines and said the report contains a current finding and recommendation regarding noncompliance with North Dakota Century Code Section 4-10.1-16 relating to penalties for late filings. He said the same finding and related recommendation was also included in the prior audit report.

Ms. Diane Peycke, Potato Council, said the Potato Council has addressed the finding and related recommendation contained in the audit report. She said the council has sent letters to potato handlers informing them that the council will begin complying with the Century Code provisions to assess penalties and interest on late filers. She said this change was implemented during the last quarter. She said in addition the Potato Council is planning on introducing legislation during the next session to change the penalty and interest provisions from being mandatory to being optional and applied at the council's discretion.

It was moved by Representative Skarphol, seconded by Senator Mutch, and carried that the committee accept the following reports:

- **For the years ended June 30, 1997 and 1996**
Development Fund, Inc.
Board of University and School Lands
Workers Compensation Bureau
Technology Transfer, Inc.
- **For the two years ended June 30, 1996**
Potato Council

Voting "aye" were Representatives Timm, Aarsvold, Byerly, Dorso, Gerntholz, Kunkel, Maragos,

Mickelson, Poolman, Skarphol, Wald, and Wilkie and Senators Lips, Mutch, Solberg, and Wogsland. No negative votes were cast.

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

Mr. Nagel presented the International Peace Garden, Inc., audit report for the two years ended December 31, 1996. He reviewed the auditor's responses to the committee's guidelines and said the report contains six findings and related recommendations. He said the report contains a qualified opinion due to the omission of fixed assets, the omission of expenses recorded by functional category, and the nonconversion of amounts into one functional currency.

Mr. Nagel said the first finding relates to the client not converting account balances and transactions into one functional currency in accordance with generally accepted accounting principles. He said the second finding relates to a lack of accounting records to enable expenses to be reported by functional classification and to correctly classify net assets. He said the third finding relates to inadequate fixed asset records. Mr. Nagel said the fourth finding relates to the need for the development and implementation of policies regarding allowable business and travel expenses and the required documentation for these expenses. He said the fifth finding relates to the proper approval and review of supporting documents for travel and credit card expenses. He said the sixth finding relates to a lack of internal controls surrounding chapel collections.

Mr. John Grettum, State Auditor's office, presented the Bismarck State College audit report for the years ended June 30, 1997 and 1996. He reviewed the auditor's responses to the committee's guidelines and said the report contains two findings and related recommendations. He said the first finding relates to refunds of appropriated expenditures and the second finding relates to trade-ins of equipment.

Mr. Grettum presented the University of North Dakota - Williston audit report for the years ended June 30, 1997 and 1996. He reviewed the auditor's responses to the committee's guidelines and said the report contains two findings and related recommendations. He said the first finding relates to refunds of appropriated expenditures and the second finding relates to maintaining fixed asset inventory records.

Mr. Grettum presented the North Dakota State University audit report for the years ended June 30, 1997 and 1996. He reviewed the auditor's responses to the committee's guidelines and said the report contains three findings and related

recommendations. He said the first finding relates to the lack of proper documentation for lease versus purchase analyses. He said the second finding relates to refunds of appropriated expenditures and the third finding relates to payments made between the Main Research Station and North Dakota State University.

Mr. Grettum presented the State College of Science audit report for the years ended June 30, 1997 and 1996. He reviewed the auditor's responses to the committee's guidelines and said the report contains two findings and related recommendations. He said the first finding relates to trade-ins of equipment and the second finding relates to refunds of appropriated expenditures.

Mr. Grettum presented the Dickinson State University audit report for the years ended June 30, 1997 and 1996. He reviewed the auditor's responses to the committee's guidelines and said the report contains three findings and related recommendations. He said the first finding relates to the proper approval of journal entries, the second finding relates to the disposal of interdepartmental billings, and the third findings relates to refunds of appropriated expenditures.

Mr. Grettum presented the Mayville State University audit report for the years ended June 30, 1997 and 1996. He reviewed the auditor's responses to the committee's guidelines and said the report contains one finding and related recommendation. He said the finding relates to the lack of proper documentation of lease versus purchase analyses.

Mr. Grettum presented the Minot State University audit report for the years ended June 30, 1997 and 1996. He reviewed the auditor's responses to the committee's guidelines and said the report does not contain any findings or recommendations.

It was moved by Senator Lips, seconded by Representative Aarsvoid, and carried that the committee accept the following reports:

- **For the two-year period ended December 31, 1996**
 - International Peace Garden**
- **For the years ended June 30, 1997 and 1996**
 - Bismarck State College**
 - UND-Williston**
 - North Dakota State University**
 - State College of Science**
 - Dickinson State University**
 - Mayville State University**
 - Minot State University**

Voting "aye" were Representatives Timm, Aarsvold, Byerly, Dorso, Gerntholz, Kunkel, Maragos, Mickelson, Poolman, Skarphol, Wald, and Wilkie and Senators Lips, Mutch, Solberg, and Wogsland. No negative votes were cast.

Mr. Grettum presented the North Dakota University System audit report for the year ended June 30, 1997. He said the report contains an unqualified opinion. He reviewed the auditor's responses to the committee's guidelines and said the report contains four findings and related recommendations. He said the first finding relates to North Dakota State University, Mayville State University, Valley City State University, and Minot State University not complying with North Dakota Century Code Section 54-27-21.1 and Board of Higher Education Policy 804 relating to documenting lease versus purchase analyses for equipment and personal property. He said the recommendation is that these institutions comply with the Century Code and the board policy. He said the State Auditor's office is working with the University System to develop an easier, less complicated lease versus purchase worksheet.

Mr. Grettum said the second finding relates to an agency fund the University System established on the University of North Dakota's general ledger. He said because the fund is used for systemwide projects it should not be classified on the University of North Dakota's general ledger. Mr. Grettum said the State Auditor's office is recommending that the University System properly record and classify activity for the development of a new computer system. He said the recommendation is also that the University System includes the expenditures associated with the administrative systems project in the budgets presented to the Board of Higher Education and the Legislative Assembly.

Mr. Grettum said the third finding relates to the proper recognition of accounts receivable. He said the State Auditor's office recommends that the University of North Dakota establish an allowance for doubtful accounts for each fund for which it believes a portion of the receivables may be uncollectible, obtain adequate supporting documentation for establishing accounts receivable, and examine its credit granting and collection policies and procedures related to the Medical School.

Mr. Grettum said the fourth finding relates to travel expenditure internal controls at North Dakota State University. He said the recommendation of the State Auditor's office is that North Dakota State University require proper supporting documentation for all expenditures and that the

expenditures comply with university policies. He said they also recommend that only allowable and reasonable expenditures associated with the intent of the trip be paid and that coaches and department heads be reimbursed in accordance with North Dakota Century Code Section 44-08-04, appropriate North Dakota State University policies, and the Office of Management and Budget's fiscal management travel policies by properly completing travel vouchers for all employee travel. He said the recommendation also stated that proper authorization should be obtained for all out-of-state travel in accordance with the Century Code and Board of Higher Education policy.

Mr. Grettum reviewed Note 20 of the financial statements regarding deficit fund balances in excess of \$100,000. He said Minot State University, the University of North Dakota, and Valley City State University had deficit fund balances totaling \$662,615, \$6,037,851, and \$163,838, respectively.

Representative Dorso asked why the Legislative Audit and Fiscal Review Committee had not been informed of some of the findings and recommendations included in the management letters sent to the universities. Mr. Grettum said whenever a management letter is provided to a client it is noted in the audit report that such a letter was distributed. He said the issues contained in the management letters are immaterial issues. He said if an issue was to become material, it would be disclosed in the audit report. He said copies of the management letters are available to anyone upon request.

Representative Dorso said the issues in the management letters to the University of North Dakota are now being brought to this committee after a number of years of only being disclosed to the board and the institution. He said maybe the committee should start requesting copies of these letters. Mr. Grettum said in the past the State Auditor's office has been criticized for putting immaterial issues in the audit reports because the reports lose their effectiveness when immaterial findings and recommendations are included. He said because of that criticism the State Auditor's office started excluding immaterial findings from the audit reports and started reporting them in management letters.

In response to a question from Representative Skarphol, Mr. Grettum said the management letters are only distributed to the client. He said in the case of higher education institutions a copy of the letter is provided to the board office and the institution. He said the letters are also available to anyone else upon request.

Representative Maragos asked if any illegal actions have taken place in regard to the issues contained in the University System audit report. Mr. Grettum said the State Auditor's office would have stated in its report if it thought illegal actions had taken place. He said the report does not state that and in his opinion all of the issues in the report should be looked upon as accounting issues.

Representative Dorso said in his opinion negative fund balances that are properly disclosed are not a problem. He said the problem occurs when negative fund balances are hidden and not properly disclosed.

In response to a question from Representative Dorso, Mr. Grettum said the issue of improperly transferring between funds to cover deficits was disclosed in management letters sent to the University of North Dakota and the board office.

In response to a question from Representative Dorso, Mr. Larry Isaak, Chancellor, North Dakota University System, said he was unaware of the fund deficits at the Medical School.

Representative Dorso said many of the problems in higher education seem to be related to capital building projects. He said the institutions seem to have difficulty staying within budget on capital projects and in complying with capital building plans as explained to the Legislative Assembly. He said the Board of Higher Education needs to develop ways to provide assurance that future capital project budgets will be more closely adhered to.

Representative Dorso said the Legislative Assembly has made a great effort toward building a trusting relationship with the higher education system. He said he does not know how much longer this progress can proceed if the financial information provided by the University System cannot be relied on by the Legislative Assembly. He said the board needs to take significant steps to make sure that these types of things do not happen again.

Mr. Isaak said the board is as concerned about this issue as are legislators. He said the board has approved a plan for the Medical School to repay the deficit fund balances over the next few years. He said having the trust of the Governor, legislators, and citizens is very important to the higher education system. Mr. Isaak said the board is currently looking at capital project policy changes which would require the institutions to periodically report to the board on revenues and expenditures throughout the term of the project. He said the reports would compare actual and projected revenues and expenditures throughout the term of the project.

Representative Aarsvold asked if there was a reason for any of the institutions without deficit balances to be concerned about future appropriation levels. Mr. Isaak said the fact that some institutions have to spend down reserves will likely leave less flexibility throughout the system.

Representative Wald said the performance audit to be presented later indicates that there is an 85 percent noncompliance rate with the board's policy regarding construction change orders. He said with this high of a noncompliance rate legislators may not believe that future board policies will be adhered to more strictly. Representative Wald said it is important for the board to begin taking a more active leadership role. He expressed concern regarding the recent lack of leadership demonstrated by the board.

Dr. Kendall Baker, President, University of North Dakota, said the Board of Higher Education recently approved a resolution addressing the deficit fund balances at the University of North Dakota Medical School. He said the deficits will be paid from Medical School resources and from proceeds from the sale of the rehabilitation hospital. He said the deficit fund balances should be eliminated by February 1, 1998, or shortly thereafter. Dr. Baker said funds loaned to the Medical School will then be paid back over a period of three years through other funds generated by the Medical School.

Dr. Baker said the university has reviewed its fund balances and does not foresee any new deficit balances arising. He said some of the current deficit fund balances will continue for a few years until the deficit is entirely repaid.

Representative Byerly indicated that North Dakota Century Code Sections 12.1-11-02 and 12.1-11-05 relate to false statements and tampering with public records. He said in his opinion somebody at the University of North Dakota is guilty of either a Class A misdemeanor or a Class C felony because of the transferring of money between funds. Dr. Baker said no employee was intentionally or deliberately trying to act in an illegal fashion. He said there was an agreement between the university and the Medical School regarding the deficit fund balances. He said because of that agreement transfers were made to reflect the agreement in the fund accounting records.

Representative Dorso said the auditor's office indicated that management letters addressed this practice for more than one year and that the procedure was not stopped immediately. Dr. Baker said the management letters did not specifically address the Medical School's funds until 1996. He said after that time the transfer of

funds was discontinued and that is why the deficit balances now appear in the 1997 financial statements.

Ms. Peggy Lucke, University of North Dakota, said at the time the Medical School incurred the deficit fund balances it had adequate moneys in other funds to cover the deficits. She said the decision was made to not deplete the Medical School reserves but to transfer between funds until the deficit could be repaid. Ms. Lucke said the accounting transactions to transfer funds was not an attempt to deceive or cover up anything but was an attempt to more accurately reflect the financial position of the funds. She said the first management letter received by the university which was specific to the entries regarding the Medical School transfers was received in 1996. She said after that time the transactions were discontinued and that is why the deficit appeared in the 1997 financial statement.

Senator Wogsland said the auditor's reports contain responses to specific questions developed by this committee. He said one of the questions to be answered by the auditors in every audit is whether there were any indications of fraud or dishonesty. He said the North Dakota University System financial report indicates that there were no indications of fraud or dishonesty. Senator Wogsland asked if that is still the position of the State Auditor's office. Mr. Grettum said the position of the State Auditor's office has not changed since the issuance of the report.

It was moved by Senator Solberg, seconded by Representative Skarphol, and carried that the Legislative Audit and Fiscal Review Committee not accept the June 30, 1997, North Dakota University System audit report and that the institutions with deficit fund balances present information to the committee at a future meeting on the progress of resolving the deficit fund balances.

Representative Maragos said the committee has no reason to not accept this audit. He said there is nothing wrong or incorrect in the audit report and that the deficit fund balances would be reviewed and addressed during following audits.

Voting "aye" were Representatives Timm, Byerly, Dorso, Gerntholz, Skarphol, and Wilkie and Senators Mutch and Solberg. Voting "nay" were Representatives Kunkel, Maragos, Mickelson, Poolman, and Wald and Senators Lips and Wogsland.

Mr. Don LaFleur, State Auditor's office, presented the University of North Dakota computer center general controls audit for the period ended October 9, 1997. A copy of the report is on file in the Legislative Council office.

He said the prior audit of the University of North Dakota computer center included 12 recommendations. He said three of the 12 recommendations have not been implemented and are included in the recommendations contained within this report. Mr. LaFleur said this report contains 11 recommendations relating to the general controls which were in place at the University of North Dakota computer center during the period from July 1, 1996, until October 9, 1997. Mr. LaFleur reviewed the recommendations contained in the report. A copy of the recommendations is attached as Appendix B.

It was moved by Representative Maragos and seconded by Senator Lips that the committee table the performance audit report on state procurement practices of the North Dakota University System until its next meeting.

Mr. Gordy Smith, State Auditor's office, said the staff person who was the auditor in charge of this audit is leaving employment with the state of North Dakota to accept employment with another state and will not be available at the next meeting should questions arise on the report. He said because of this he would prefer that the committee not delay presentation of the report.

The motion and second were withdrawn.

Representative Maragos said he received a letter from Mr. Nagel of the State Auditor's office informing him that audit reports are available to the public upon request once the report is finalized by the State Auditor's office. He said it has been his understanding that in the past reports have not been released to the public until the report was presented to the Legislative Audit and Fiscal Review Committee. Representative Maragos said he is concerned with the change in policy by the State Auditor's office because it allows for the press and others to generate a substantial amount of publicity regarding certain audit issues before members of this committee have a chance to receive the report.

Mr. Nagel said the previous policy of the State Auditor's office was to review audit reports with agencies prior to being presented to this committee. He said this policy was based upon a recommendation by this committee that agencies be asked to respond to the audit findings before the reports were presented to the Legislative Audit and Fiscal Review Committee. He said based on changes made to the open records law by the 1997 Legislative Assembly, this policy is no longer allowable under the current Century Code provisions. Mr. Nagel said because of the changes made by the 1997 Legislative Assembly, the State Auditor's office requested the Attorney General's office to determine when audit reports

were required to be released to the public. He said based on the Attorney General's office, the audit report is treated differently than the audit working papers. He said working papers are confidential and not subject to the open records law. Mr. Nagel said based on the Attorney General's office, audit reports become public after the report is through the quality control process of the State Auditor's office and no significant changes are anticipated. He said based on this the State Auditor's office has changed its policy and now makes reports available to the public when completed.

Representative Maragos expressed concern with changes made during the last legislative session which now require the auditor's office to release audit reports prior to the report being presented to this committee.

It was moved by Representative Maragos, seconded by Representative Poolman, and carried that the Legislative Council staff prepare and present at the next meeting a bill draft to provide that performance audit reports and financial audit reports prepared by the State Auditor's office are exempted from the open records law until the report is presented to the Legislative Audit and Fiscal Review Committee. Voting "aye" were Representatives Byerly, Dorso, Gerntholz, Maragos, Mickelson, Poolman, Skarphol, Wald, and Wilkie and Senators Lips, Mutch, and Solberg. No negative votes were cast.

Vice Chairman Solberg announced that the following agenda items would be carried over to the next meeting:

1. Presentation by the Legislative Council staff of a memorandum on commodity group procedures relating to the auditing of handlers, collection procedures, and the assessment of penalties and interest.
2. Presentation by the Legislative Council staff of a memorandum on South Dakota's commodity group procedures relating to the auditing of handlers and the collection of assessments.
3. Presentation by the Legislative Council staff of a bill draft creating a centralized commodity group collection process and auditing procedures and to exclude the commodity groups from Central Personnel and Central Services requirements.
4. Presentation by the Legislative Council staff of a memorandum on the eligibility requirements for political subdivision and other organizations' participation in the Public Employees Retirement System, state fire and tornado fund, risk

management fund, and the state bonding fund.

5. Presentation by a representative of the Department of Human Services on its accounts receivable writeoffs and a report on:
 - a. The aging of the accounts receivable writeoffs relating to Indian Health Service.
 - b. Collection efforts utilized on the amounts to be written off.
 - c. The agreement between the Department of Human Services and Indian Health Service, including the Indian Health Service payment requirements for services provided.
 - d. The department's policy regarding the provision of services when the ability to pay does not exist.
 - e. The provisions of the *White v. Califano* case relating to the different Indian Health Service payment requirements for American Indians living on or off a reservation.
6. Presentation by a representative of the Attorney General's office on recommended statutory changes regarding the complete disclosure of all internal service funds and how the funds within the internal service funds are spent.
7. Presentation by a representative of the Bank of North Dakota regarding options for the Bank to transfer the assets and liabilities of the beginning farmer revolving loan fund to the Bank and discontinue the need to have a separate audited financial statement.
8. Presentation by a representative of the Department of Public Instruction on the status of the foundation aid program payments.
9. Presentation by the Legislative Council staff of a bill draft on the acquisition of assets and services through financing activities by state agencies and institutions.
10. Presentation by the Legislative Council staff of a copy of the Minnesota law creating a statewide centralized collection agency.
11. Presentation by the Legislative Council staff of a memorandum on how audit findings and recommendations can be reported to the Appropriations Committees during the legislative session following the report presentation date.

Mr. Smith presented the performance audit report of state procurement practices - North Dakota University System. A copy of the report is on file in the Legislative Council office. He said the performance audit was conducted at the request of the Legislative Audit and Fiscal Review Committee. He said the focus of the performance audit in regard to the higher education institutions was on North Dakota State University, University of North Dakota, Minot State University, and State College of Science. He said these four universities were selected because they represent approximately 87 percent of the University System's purchasing.

Mr. Smith reviewed the recommendations contained in the performance audit. A copy of the recommendations is attached as Appendix C.

Representative Poolman asked why the report referenced University of North Dakota's hiring of a lobbyist but did not reference the lobbyist retained by North Dakota State University. Mr. Smith said the expenditures for this were not found during the auditing procedures conducted for the performance audit. He said after his inquiry, the Fargo State Auditor's staff informed him that North Dakota State University did not retain a lobbyist.

Mr. Richard Rayl, North Dakota State University, said North Dakota State University first retained a lobbyist in about 1991. He said this lasted for about one year. Mr. Rayl said approximately three years ago the university again started contracting with a lobbyist.

In response to a question from Representative Wald, Mr. Rayl said the price of the lobbyist is cost-effective when you consider the amount of research dollars generated. He said the university does not use appropriated funds to pay the lobbyist's fees.

Representative Dorso asked if it would be possible for the University System to have one lobbyist, thereby making it more cost-effective for the system as a whole. Mr. Rayl said North Dakota State University was previously in a consortium but found that the lobbyist was not as successful when working for more than one institution. He said it is his understanding that the board office has indicated that it will look into this and determine whether or not each university should have their own lobbyist or if the system should have one lobbyist.

Mr. Isaak said the board plans on reviewing the performance audit at a future meeting. He said the board also plans on having bills drafted as necessary regarding the recommendations contained in the performance audit.

Representative Dorso suggested that the board may want to consider the possibility of having internal auditors in the board office. Mr. Isaak said more of the audits relating to higher education are containing more and more recommendations and all of these recommendations take time and financial resources. He said he is currently not in favor of adding another layer of bureaucracy within the board office. He said the cost benefit of some of the recommendations needs to be considered before the recommendations are implemented.

Ms. Laura Glatt, North Dakota University System office, said the board will be reviewing the recommendations contained in the various audit reports presented today. She said substantial amounts of staff time and resources are used to coordinate and implement the various audit recommendations. She said one example is the recommendation to discontinue vendors that are not able to accommodate the entire University System. She said the North Dakota University System cannot exclude North Dakota vendors simply because they cannot enter into purchasing contracts to serve the entire University System. She said if the University System were to do this, it would generate a substantial amount of negative publicity with the North Dakota business community.

Mr. Rod Backman, Office of Management and Budget, said for the most part the Office of Management and Budget agrees with the recommendations contained in the performance audit and is working with the North Dakota University System. He said he strongly disagrees with the recommendation that the Office of Management and Budget comply with North Dakota Administrative Code Section 4-03-15-01 by obtaining written statements from vendors who appeal state purchasing decisions. He said in the instance cited, he thinks the way the issue was handled by the Office of Management and Budget was the correct way to handle it.

Representative Dorso said it is fine to disagree with an audit recommendation, but it is not all right to simply ignore the recommendation. He said agency personnel need to do what they think is necessary, whether it means implementing a change in the Administrative Code, Century Code, or requesting an Attorney General's opinion.

It was moved by Representative Dorso, seconded by Representative Gertholz, and carried that the Legislative Audit and Fiscal Review Committee accept the following reports:

- **For the period dated October 9, 1997
University of North Dakota computer
center general controls audit**

- **For the period dated December 15, 1997 Performance audit report of state procurement practices - North Dakota University System**
- **Audit reports available but not selected for presentation to the committee**
 - Housing Finance Agency (June 30, 1997 and 1996)**
 - North Dakota Building Authority (June 30, 1997 and 1996)**
 - North Dakota Real Estate Trust (June 30, 1997 and 1996)**
 - PACE fund (June 30, 1997 and 1996)**
 - Ag PACE fund (June 30, 1997 and 1996)**

Voting "aye" were Representatives Timm, Byerly, Dorso, Gerntholz, Mickelson, Poolman, Skarphol, Wald, and Wilkie and Senators Mutch and Solberg. No negative votes were cast.

Mr. Smith presented a report on regional planning councils' intentions regarding the formation of nonprofit corporations. A copy of his presentation is on file in the Legislative Council office. He said at the July 9, 1997, meeting of the Legislative Audit and Fiscal Review Committee, a request was made for the State Auditor's office to review the most current financial audit report of the Lake Agassiz Regional Planning Council and to interview staff to determine why the Lake Agassiz Regional Planning Council may be forming a foundation. He said in addition, the committee later requested that the State Auditor's office survey the other regional planning councils to determine if any were contemplating taking similar action.

Mr. Smith said the most recent financial audit of the Lake Agassiz Regional Planning Council was reviewed. He said in addition, it was determined that the Lake Agassiz Regional Planning Council did not form a new nonprofit foundation but did rename its existing nonprofit corporation, which had been formed in 1987. He said the renaming came in July 1997 and with the renaming came an expanded scope of activities, amended bylaws, and expanded board membership. He said the Lake Agassiz Regional Planning Council transferred the assets and responsibilities for the vast majority of its programs to the separate corporation in July 1997. He said although the Lake Agassiz Regional Planning Council indicated that the programs have been contracted out to the corporation, the State Auditor's office could not find written contracts between the Lake Agassiz Regional Planning Council and the corporation.

Mr. Smith said an Attorney General's opinion stated that regional planning councils could not form nonprofit corporations. He said, however, it

also stated that those regional planning councils which are incorporated as nonprofit corporations prior to 1977 enjoy a dual status enabling them to function as a nonprofit corporation as well as a political subdivision. He said information received from Lake Agassiz Regional Planning Council's executive director and attorney contradicted each other with one saying the Lake Agassiz Regional Planning Council was formed in 1972 and the other saying it was formed as a nonprofit corporation in 1973.

Mr. Smith said the Attorney General's opinion also concluded that regional planning councils may not transfer powers and duties involving judgment and discretion to a separate nonprofit corporation. He said the opinion states that regional planning councils may otherwise contract with nonprofit corporations for the performance of certain duties.

Mr. Smith said it appears that the Lake Agassiz Regional Planning Council has taken action which changed the council's duties and responsibilities and transferred the majority of its assets to the corporation. He said based on information received from the Attorney General's office he questions whether the Lake Agassiz Regional Planning Council has the authority to pursue this course of action. He said it appears the lack of documentation brings into question the propriety and legality of some of the actions.

Mr. Smith said based on the results of the survey of the other seven regional planning councils, none indicated the intent to change the responsibilities of the regional planning council or transfer the assets to a nonprofit corporation. He said when surveyed, none of the other seven regional planning councils indicated that the legislation passed by the 1997 Legislative Assembly, which made regional planning councils political subdivisions, has had an impact on their operations.

Representative Dorso said the Attorney General's office should look into this to determine if any illegal actions have taken place since it appears the Lake Agassiz Regional Planning Council is doing things which an Attorney General's opinion said it should not.

It was moved by Representative Dorso, seconded by Representative Skarphol, and carried that the Legislative Audit and Fiscal Review Committee request the Attorney General's office to determine:

- **If the Lake Agassiz Regional Planning Council inappropriately formed a separate nonprofit corporation;**
- **If the Lake Agassiz Regional Planning Council inappropriately transferred**

powers and duties to a separate nonprofit corporation; and

- **If the Lake Agassiz Regional Planning Council inappropriately transferred funds or money to a separate nonprofit corporation.**

Senator Wogsland suggested that before the Attorney General's office is requested to investigate the Lake Agassiz Regional Planning Council, a representative of the council be invited to this committee's next meeting to answer questions. He said if the committee is not satisfied with the answers, it could then have the Attorney General's office investigate. Chairman Timm indicated that the Lake Agassiz Regional Planning Council could be invited to the next meeting.

Representative Dorso said based on the information provided today, the committee does not need to hear from the Lake Agassiz Regional Planning Council before the Attorney General begins to look into the transfers between the planning council and the nonprofit corporation.

Voting "aye" were Representatives Timm, Byerly, Dorso, Gerntholz, Mickelson, Poolman,

Skarphol, Wald, and Wilkie and Senators Mutch and Solberg. Voting "nay" was Senator Wogsland.

It was moved by Representative Poolman, seconded by Representative Skarphol, and carried on a voice vote that the meeting be adjourned. The meeting was adjourned at 6:00 p.m.

Paul R. Kramer
Senior Fiscal Analyst

Chester E. Nelson, Jr.
Legislative Budget Analyst and Auditor

ATTACH:3