

NORTH DAKOTA LEGISLATIVE COUNCIL

Minutes of the

LEGISLATIVE AUDIT AND FISCAL REVIEW COMMITTEE

Tuesday, October 5, 1999
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, Rex R. Byerly, RaeAnn G. Kelsch, Doug Lemieux, Andrew G. Maragos, Jim Poolman, Lonny B. Winrich; Senators Dwight C. Cook, Jerry Klein, David O'Connell, Ken Solberg

Members absent: Representatives Wesley R. Belter, Ronald Nichols, Mike Timm; Senators Jerome Kelsh, Ralph Kilzer, Duane Mutch

Others present: See attached appendix

It was moved by Representative Poolman, seconded by Representative Kelsch, and carried on a voice vote that the minutes of the July 13, 1999, meeting of the Legislative Audit and Fiscal Review Committee be approved as distributed.

Mr. Ed Nagel, State Auditor's office, presented the Protection and Advocacy Project audit report for the year ended June 30, 1998. He reviewed the auditor's responses to the committee's guidelines and said the report does not contain any findings or recommendations.

Mr. Nagel presented the Milk Marketing Board audit report for the two-year period ended June 30, 1998. 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 questions from committee members, Mr. John Weisgerber, Executive Director, Milk Marketing Board, explained the fines levied on milk bottlers relating to providing illegal discounts to grocery stores. Mr. Weisgerber said there are currently six bottlers in the state, including Cass Clay locations.

Mr. Nagel presented the Potato Council audit report for the two-year period ended June 30, 1998. Mr. Nagel said the findings and recommendations relate to the Potato Council's failure to comply with North Dakota Century Code Section 4-10.1-16 regarding accessing penalties and interest required on assessments not filed by the due date and inadequate procedures surrounding expenditures. Mr. Nagel said the executive director of the Potato Council acknowledges the recommendations and will follow proper procedures in the future.

Ms. Diane Peycke, Executive Director, Potato Council, said Senate Bill No. 2292 was approved by

the 1999 Legislative Assembly to allow rather than require the Potato Council to assess penalties and interest on late filed assessments. She said the concerns and findings relating to inadequate documentation for expenditures will be corrected.

Mr. Nagel presented the Wheat Commission audit report for the two-year period ended June 30, 1998. 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, Ms. Ellen Huber, Wheat Commission, said the professional services line item included in the audit report includes funds for marketing, export services, and national wheat promotion.

In response to a question from Representative Lemieux, Ms. Huber said the Wheat Commission is authorized to use up to two mills of its wheat tax levy for trade issues.

In response to a question from Representative Byerly regarding producer refunds, Ms. Huber said the North Dakota Century Code requires the Wheat Commission to receive in writing a request for a refund request form from a producer, at which time the Wheat Commission provides a refund request form to the producer who then has 60 days to file for the refund. Representative Byerly said problems are encountered when people request the refund forms by e-mail, telephone, or fax. He suggested the Wheat Commission review this process to update, if necessary, the North Dakota Century Code for today's business practices.

Mr. Nagel presented the Barley Council audit report for the two-year period ended June 30, 1998. He reviewed the auditor's responses to the committee's guidelines and said the report does not contain any findings or recommendations.

Mr. Nagel presented the State Seed Department audit report for the two-year period ended June 30, 1998. He reviewed the auditor's responses to the committee's guidelines and said the auditor's findings and recommendations include recommendations that the Seed Department receive Emergency Commission approval prior to exceeding 75 percent of the salaries and wages line item during the first 18 months of a biennium to adequately identify equipment inventory and to have adequate voucher

approval. The Seed Department agreed with the related recommendations and have made the necessary changes.

In response to a question from Representative Aarsvold, Mr. Ken Bertsch, Seed Department, said the reason the Seed Department exceeded 75 percent of its appropriation for salaries and wages on December 31, 1996, was because of two issues requiring a large expenditure of salaries and wages, the karnal bunt testing effort and shipping point inspections for potatoes. He said the department's salaries are typically seasonal with the largest expenditures from June to December of each year. He said the Seed Department did receive approval after the fact and will receive prior Emergency Commission approval in the future.

Mr. Paul Trauger, Certified Public Accountant, presented the State Board of Cosmetology audit report for the fiscal year ended June 30, 1998. He reviewed the auditor's responses to the committee's guidelines and said the report contains a recommendation that the official board minutes contain motions and recorded roll call votes.

In response to questions from Senator O'Connell, Ms. Bert Knell, State Board of Cosmetology, said the board has addressed its past financial problems and although it has approximately \$46,000 in investments, it feels that amount is necessary as a cushion in the event that all license fees are not collected.

Mr. Ronald Tolstad, Jr., State Auditor's office, provided testimony regarding the State Auditor's office strategic plan and plans to change the audit standards used in reports prepared for the Legislative Audit and Fiscal Review Committee, a copy of which is on file in the Legislative Council office. Mr. Tolstad reviewed the financial statement audit standards that are currently used and the performance audit standards that are to be followed beginning January 1, 2000. Financial statement audits generally must be prepared in accordance with generally accepted accounting principles, while performance audits provide an assessment of governmental performance and include economy and efficiency audits. He said the performance audit standards are more applicable and provide several advantages to the financial audit standards. He said performance audit standards would also include audited financial statements in the reports to the Legislative Audit and Fiscal Review Committee. He said, however, an opinion would not be issued on the financial statements as performance audit standards do not determine if the statements are prepared in accordance with generally accepted accounting principles. Later in the meeting, Mr. Tolstad also provided an example of a template report that would be used in the State Auditor's office biennial audit reports, a copy of which is on file in the Legislative Council office.

The committee discussed the proposed change. Representative Maragos said he is concerned with

changing the standards so quickly and that an opinion on the financial statements would not be issued by the State Auditor's office.

Mr. Tolstad said the financial auditing standards are not an exact fit and the performance audit standards would allow the State Auditor's office to spend more time looking at agency compliance with legislative intent.

Mr. Chester E. Nelson, Jr., Legislative Budget Analyst and Auditor, said he has met with representatives of the State Auditor's office on several occasions and emphasized that the financial statements are an important part of the State Auditor's office audit reports. He said the readers of the audit reports expect to have audited amounts reflected in the financial statements. He said he is concerned that if audited financial statements are not required, agencies may believe that financial data is not important.

Representative Maragos said he is concerned with the proposed changes and the fact that the issue was not addressed during the 1999 Legislative Assembly.

Representative Byerly said it appears that the audit reports issued under the new standards would answer many of the questions that legislators have and he had no problem with the proposed change. Senator Solberg said he supports the proposed change.

Mr. Nelson suggested that the State Auditor's office prepare a statement for the committee's consideration expressing support for the proposed change and including a reference to audited financial statements.

It was moved by Senator Solberg, seconded by Senator Klein, and carried that the Legislative Audit and Fiscal Review Committee support the office of the State Auditor's plans to change from financial statement audit standards to performance audit standards for biennial audits subject to the continuation of providing reliable audited financial statements in the biennial audit reports. Representatives Wald, Byerly, Kelsch, Lemieux, and Poolman and Senators Cook, Klein, and Solberg voted "aye." Representatives Aarsvold and Winrich and Senator O'Connell voted "nay."

Mr. Alton Nitschke, Eide Bailly LLP, Certified Public Accountants, presented the State Fair Association audit report for the years ended September 30, 1998 and 1997. He reviewed the auditor's responses to the committee's guidelines and said the report recommends that the State Fair Association obtain an Attorney General's opinion relating to the depositing of sales tax moneys collected by the city of Minot in an account used for State Fair arena expansion projects. The North Dakota Century Code requires that moneys collected by the State Fair Association be deposited in the Bank of North Dakota. He said the report contains an unqualified opinion.

In response to a question from Representative Byerly regarding the lease arrangement with Flat

Trac, Inc., and the potential state liability, Mr. Gerald Iverson, Manager, State Fair Association, said the contract with the track operators requires insurance liability coverage to protect the interests of the State Fair Association. He said the certificate of insurance includes a \$1 million liability limit.

Mr. Nitschke presented the beginning farmer revolving loan fund audit report for the years ended December 31, 1998 and 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 a qualified opinion relating to year 2000 disclosure issues.

Mr. Nitschke presented the community water facility loan fund audit report for the years ended December 31, 1998 and 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 a qualified opinion relating to year 2000 disclosure issues.

Mr. Nitschke presented the Municipal Bond Bank audit report for the years ended December 31, 1998 and 1997. He reviewed the auditor's responses to the committee's guidelines. He said the report includes findings relating to segregation of accounting functions necessary to ensure adequate internal control and because the Municipal Bond Bank has determined the cost benefit of adding another staff member is not an option, procedures have been and will continue to be implemented to provide the highest level of internal control possible. He said the report contains a qualified opinion relating to year 2000 disclosure issues.

Mr. Nitschke presented the developmentally disabled facility loan fund audit report for the years ended December 31, 1998 and 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 a qualified opinion relating to year 2000 disclosure issues.

The committee recessed at 12:11 p.m. and reconvened at 1:15 p.m.

Mr. Don Wolf, Donald R. Wolf & Associates, P.C., presented the Stockmen's Association audit report for the years ended December 31, 1998 and 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.

In response to a question from Representative Wald regarding out-of-state investments, Mr. Wade Moser, Director, Stockmen's Association, said the Stockmen's Association does have investments in out-of-state banks to realize the highest rate of return possible.

Ms. Kathy Grafsgaard, Department of Public Instruction, provided testimony regarding the lawsuit involving Dakota Nutrition, Inc. She discussed the history of Dakota Nutrition, an entity providing federal funding to day care providers in the Minot area for meal reimbursement. She said in mid-1997 the Department of Public Instruction became concerned because audits were not filed timely and corrective action was not taken by Dakota Nutrition. In December 1997 Dakota Nutrition ceased operations and an accounting firm was hired to audit Dakota Nutrition. The auditing firm found approximately \$1.4 million of audit exceptions, where documents were not available supporting payments received by Dakota Nutrition from the Department of Public Instruction and provided day care providers for nutritional meals. She said the department has sought a partial default judgment of \$12,438 relating to inappropriate administrative expenses claimed by Dakota Nutrition. She said the department does not believe that the \$1.4 million of audit exceptions was used for anything other than payments to day care providers for meals and the audit exceptions were a result of a lack of adequate records. She said recipients have not come forward and indicated that they did not receive the payments that they were entitled.

Senator Cook distributed a copy of a Legislative Council memorandum entitled *Child and Adult Care Food Program - Administration and Federal Funds Received for 1995-97 and 1997-99 Biennium*. Senator Cook questioned the Department of Public Instruction procedures for auditing these agencies that provide payments to day care centers. In response, Ms. Grafsgaard said the Department of Public Instruction now contracts for audits on an annual basis rather than allowing the provider to contract for its own audits.

Senator Solberg said there was a 26-month delay in the audits and questioned why Dakota Nutrition was allowed to continue doing business. Ms. Grafsgaard said based on United States Department of Agriculture regulations, the Department of Public Instruction was not allowed to cease the operations of Dakota Nutrition but rather was required to first work with the agency to implement necessary corrective action.

Representative Poolman said the Department of Public Instruction did not act quickly enough to take the corrective action to protect the taxpayers' money.

Mr. Doug Bahr, Director, Civil Litigations Division, Attorney General's office, discussed the current status of the case. He said the Attorney General has filed a motion for a partial default judgment against the owner of Dakota Nutrition who has left the state and has not answered the previous causes of action. He said the default judgment is for the \$12,438 and does not at this time relate to the \$1.4 million.

In response to a question from Representative Wald, Ms. Grafsgaard said the number of clients remain constant after Dakota Nutrition ceased

operations, indicating that Dakota Nutrition was not claiming funds for meals that were not appropriate.

Mr. Gordy Smith, State Auditor's office, said the finding was a result of the State Auditor's office federal audit and suggested one way to verify Dakota Nutrition's expenditures would be to survey all day care providers receiving reimbursement for the 26-month period and ask them to submit copies of their claims for reimbursement to verify the amounts paid to the providers.

Senator Solberg suggested an update be provided by the Department of Public Instruction and the Attorney General's office at the committee's next meeting.

Mr. Wolf presented the audit reports for the Legislative Assembly and Legislative Council for the two-year period ended June 30, 1999 and 1998. He reviewed the auditor's responses to the committee's guidelines and said the reports do not contain any findings or recommendations. He said the reports contain unqualified opinions.

It was moved by Senator O'Connell, seconded by Senator Cook, and carried that the Legislative Audit and Fiscal Review Committee accept the Legislative Council and Legislative Assembly audit reports for the fiscal years ended June 30, 1999 and 1998. Representatives Wald, Aarsvold, Byerly, Kelsch, Lemieux, Poolman, and Winrich and Senators Cook, Klein, O'Connell, and Solberg voted "aye." No negative votes were cast.

Ms. Brenda Weisz, Department of Human Services, presented a summary of uncollectible accounts receivable as of June 30, 1999. A copy of her presentation and a detailed listing are on file in the Legislative Council office.

It was moved by Representative Byerly, seconded by Representative Poolman, and carried that the Legislative Audit and Fiscal Review Committee accept the Department of Human Services report on the writeoffs of accounts receivable as of June 30, 1999, of \$14,554,545.43 at the State Hospital, \$171,613 at the Developmental Center, and \$128,322.14 at the human service centers.

Representatives Wald, Aarsvold, Byerly, Kelsch, Lemieux, Poolman, and Winrich and Senators Cook, Klein, O'Connell, and Solberg voted "aye." No negative votes were cast.

Mr. Thomas Clifford, representing the University of North Dakota Aerospace Foundation, commented on the status of the foundation. He said the foundation currently is reviewing its status and will issue a report to President Kupchella who will make the decision regarding the future role of the Aerospace Foundation. He said the foundation is looking at various opportunities, including diversifying its customer base by negotiating training programs with other foreign countries and the possibility of a space training program at the University of North Dakota.

In response to a question from Representative Byerly, Ms. Peggy Lucke, Acting Vice President for Finance and Operations, University of North Dakota, discussed the status of the lease receivables the university has with Northwest Airlines. She said Northwest Airlines in July 1998 indicated an intent to terminate its contractual arrangement for the lease of a building on campus. She said the University of North Dakota believes that Northwest Airlines must continue to make these payments and has filed suit against Northwest Airlines to collect the lease receivables. A preliminary court date is expected in December 2000.

In response to a question from Senator Solberg, Ms. Terri Clark, Fiscal Affairs, University of North Dakota Aerospace Division, said the audit of the University of North Dakota Aerospace Foundation for the year ended June 30, 1999, should be available by the next Legislative Audit and Fiscal Review Committee meeting at which time she would share the report with the committee.

In response to a question from Representative Wald, Ms. Lucke said the University of North Dakota will be in district court on October 6, 1999, with a lawsuit against Western National Insurance regarding boiler coverage relating to payment of benefits for flood damage.

Mr. Irvin Rustad, Director, Lake Agassiz Regional Planning Council, provided testimony regarding the status of Lake Agassiz Regional Planning Council's nonprofit corporation. Mr. Rustad said the Attorney General's office ruled that a previous transfer of assets to the nonprofit corporation was inappropriate and the Attorney General's office suggested the Lake Agassiz Regional Planning Council work with the local state's attorney and local county commissioners to transfer the assets back to the regional planning council, which has been completed. He said after the transfers were completed, the regional planning council needed to replace approximately \$14,900 to make the transaction complete. He said there are now two separate organizations with two separate boards and two separate bylaws. He said the nonprofit organization is necessary to receive donations and federal funds that the regional planning council cannot receive.

Representative Poolman said the Legislative Audit and Fiscal Review Committee was following up on the Attorney General's recommendations and findings that the moneys should not have been transferred to the nonprofit organization. Representative Poolman said he is still concerned that there may be a commingling of responsibilities and staff between the two organizations.

Representative Wald asked Mr. Rustad if he had indicated to the State Auditor's office that they could not conduct an audit of the two organizations. Mr. Rustad said he had not, that he pays an accounting firm to conduct audits of the two

organizations and would invite the State Auditor's office to participate when the next annual audit is done, if that can be done without additional charge to the organizations. He said a private audit firm was chosen as the firm can also advise the organizations on financial activities.

In response to questions from Senator Solberg, Mr. Rustad said approximately \$4.5 million was originally transferred from the regional planning council to the nonprofit entity and programs have been returned to the regional planning council. He said the regional planning council needs a nonprofit organization to access funding for the federal government and other sources. Senator Solberg suggested Mr. Rustad work with other regional planning councils if a nonprofit organization is effective. He said the Legislative Audit and Fiscal Review Committee was reviewing the situation because the Lake Agassiz Regional Planning Council was perceived as attempting to avoid a state audit.

It was moved by Representative Poolman, seconded by Senator Solberg, and carried on a voice vote that the Legislative Audit and Fiscal Review Committee, subject to the approval of the Legislative Council chairman, invite representatives of the Attorney General's office to provide a status report regarding the Lake Agassiz Regional Planning Council, to conduct a followup review of the new administrative structure of the Lake Agassiz Regional Planning Council and nonprofit entity, and to comment regarding the appropriateness of the new administrative structure.

Representative Aarsvold said representatives from Traill County have indicated to him that they are pleased with the efforts of the Lake Agassiz Regional Planning Council.

Mr. Kevin Cramer, Director, Department of Economic Development and Finance, testified on the status of the legal dispute with the Lewis and Clark Regional Development Council. He said the dispute has been settled and it would now be appropriate for state agencies to do business with the Lewis and Clark Regional Development Council. He said at question were state funds provided for a nonfederal match totaling \$37,500, which has been converted to a 30-year one percent loan to match the federal loan. He said the lesson learned is that these federal funds are not compatible with state programs.

It was moved by Representative Poolman, seconded by Representative Kelsch, and carried on a voice vote that the Legislative Audit and Fiscal Review Committee request the chairman of the Legislative Council inform state agencies that the issue regarding the Lewis and Clark Regional Development Council and the North Dakota development fund has been resolved and that the Legislative Audit and Fiscal Review Committee is no longer asking agencies to comply with the motion adopted at the committee's January 27,

1999, meeting regarding agency financial activities with the Lewis and Clark Regional Development Council.

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

- **Audit reports presented to the committee:**
 - **For the year ended June 30, 1998**
 - **Protection and Advocacy Project**
 - **State Board of Cosmetology**
 - **For the years ended June 30, 1998 and 1997**
 - **Milk Marketing Board**
 - **Potato Council**
 - **Wheat Commission**
 - **Barley Council**
 - **State Seed Department**
 - **For the years ended September 30, 1998 and 1997**
 - **State Fair Association**
 - **For the years ended December 31, 1998 and 1997**
 - **Beginning farmer revolving loan fund**
 - **Community water facility loan fund**
 - **Municipal Bond Bank**
 - **Developmentally disabled facility loan fund**
 - **Stockmen's Association**
- **Audit reports available but not selected for presentation to the committee:**
 - **State Board of Public Accountancy (June 30, 1999)**
 - **State Board of Pharmacy (June 30, 1998 and 1997)**
 - **North Dakota Firemen's Association (April 30, 1999)**
 - **State Board of Chiropractic Examiners (December 31, 1998)**
 - **Board of Athletic Trainers (June 30, 1998 and 1997)**
 - **State Examining Committee of Physical Therapists (June 30, 1998)**
 - **State Board of Architecture (June 30, 1998 and 1997)**
 - **State Board of Medical Examiners (December 31, 1998 and 1997)**
 - **Board of Examiners on Audiology and Speech-Language Pathology (June 30, 1999 and 1998)**
 - **Board of Registration for Professional Soil Classifiers (June 30, 1999 and 1998)**
 - **Peace Officer Standards and Training Board (December 31, 1998, and June 30, 1998)**

Representatives Wald, Aarsvold, Byerly, Kelsch, Lemieux, Poolman, and Winrich and Senators Cook, Klein, O'Connell, and Solberg voted "aye." No negative votes were cast.

It was moved by Representative Byerly, seconded by Senator Klein, and carried that the Legislative Audit and Fiscal Review Committee request the State Auditor's office to conduct an audit of the Commission on the Future of Agriculture relating to the commission's state funding. Representatives Wald, Aarsvold, Byerly, Kelsch, Lemieux, Poolman, and Winrich and Senators Cook, Klein, O'Connell, and Solberg voted "aye." No negative votes were cast.

It was moved by Representative Lemieux that the Legislative Audit and Fiscal Review Committee request the State Auditor's office to conduct an audit of the Workers Compensation

Bureau emphasizing the review process for injured workers, legal fees, and the resolution of disputed claims. The motion was withdrawn.

The committee adjourned at 4:20 p.m.

Jim W. Smith
Assistant Legislative Budget Analyst and Auditor

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

ATTACH:1