

NORTH DAKOTA  
DEPARTMENT OF  
VETERANS AFFAIRS

FARGO, NORTH DAKOTA

**Audit Report**

For the Two-year Period Ended  
June 30, 2008

ROBERT R. PETERSON  
STATE AUDITOR

Office of the State Auditor  
Division of State Audit

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STATE OF NORTH DAKOTA  
**OFFICE OF THE STATE AUDITOR**  
STATE CAPITOL  
600 E. BOULEVARD AVENUE - DEPT. 117  
BISMARCK, NORTH DAKOTA 58505

## *Transmittal Letter*

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July 7, 2009

The Honorable John Hoeven, Governor  
Members of the North Dakota Legislative Assembly  
Mr. Lonnie Wangen, Commissioner

We are pleased to submit this audit of the North Dakota Department of Veterans Affairs for the two-year period ended June 30, 2008. This audit resulted from the statutory responsibility of the State Auditor to audit or review each state agency once every two years. The same statute gives the State Auditor the responsibility to determine the contents of these audits.

In determining the contents of the audits of state agencies, the primary consideration was to determine how we could best serve the citizens of the state of North Dakota. Naturally we determined financial accountability should play an important part of these audits. Additionally, operational accountability is addressed whenever possible to increase efficiency and effectiveness of state government.

The in-charge auditor for this audit was Robyn Hoffmann, CPA. Mary Feltman, CPA, was the staff auditor. John Grettum, CPA, was the audit manager. Inquiries or comments relating to this audit may be directed to the audit manager by calling (701) 239-7289. We wish to express our appreciation to Commissioner Wangen and his staff for the courtesy, cooperation, and assistance they provided to us during this audit.

Respectfully submitted,

A handwritten signature in cursive script that reads "Bob Peterson".

Robert R. Peterson  
State Auditor

# *Executive Summary*

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## *Introduction*

The North Dakota Department of Veterans Affairs was created under Section 37, Article 18 of the North Dakota Century Code. It is the function of the North Dakota Department of Veterans Affairs to coordinate agencies or instrumentalities of the state set up to render service and benefits to returning veterans; to have charge of and implement programs and benefits authorized by statute; to assist or represent veterans or their widows, administrators, executors, guardians, or heirs, in processing claims; to advise and assist veterans in taking advantage of the provisions of the Servicemen's Readjustment Act of 1944, or any similar or related measures afforded by the federal government; to assist, supervise, advise, and direct the work of county service officers; to assist county service officers in the formation of county service to veterans' committees and to outline, assist, and direct the activities of such committees.

North Dakota Century Code Chapter 37-18.1, created an Administrative Committee on Veterans' Affairs, which is responsible for the organization, policy, and general administration of all veterans' affairs in the state of North Dakota.

The North Dakota Department of Veterans Affairs is also authorized, under North Dakota Century Code sections 37-14-03.3 and 37-14-04, to maintain a permanent revolving fund for the purpose of making loans to qualified veterans.

The Legislative Audit and Fiscal Review Committee (LAFRC) requests that certain items be addressed by auditors performing audits of state agencies. Those items and the Office of the State Auditor's response are noted below.

## *Responses to LAFRC Audit Questions*

### *1. What type of opinion was issued on the financial statements?*

Financial statements were not prepared by the North Dakota Department of Veterans Affairs in accordance with generally accepted accounting principles so an opinion is not applicable. The agency's transactions were tested and included in the state's basic financial statements on which an unqualified opinion was issued.

### *2. Was there compliance with statutes, laws, rules, and regulations under which the agency was created and is functioning?*

Yes.

### *3. Was internal control adequate and functioning effectively?*

Other than our finding addressing the "loans receivable" (page 10), we determined internal control was adequate.

### *4. Were there any indications of lack of efficiency in financial operations and management of the agency?*

No.

5. *Has action been taken on findings and recommendations included in prior audit reports?*

The Department of Veterans Affairs has implemented all recommendations included in the prior audit report.

6. *Was a management letter issued? If so, provide a summary below, including any recommendations and the management responses.*

Yes, a management letter was issued and is included on page 14 of this report, along with management's response.

### **LAFRC Audit Communications**

7. *Identify any significant changes in accounting policies, any management conflicts of interest, any contingent liabilities, or any significant unusual transactions.*

There were no significant changes in accounting policies, no management conflicts of interest were noted, no contingent liabilities were identified or significant unusual transactions.

8. *Identify any significant accounting estimates, the process used by management to formulate the accounting estimates, and the basis for the auditor's conclusions regarding the reasonableness of those estimates.*

The North Dakota Department of Veterans Affairs' financial statements do not include any significant accounting estimates.

9. *Identify any significant audit adjustments.*

We made two audit adjustments in fiscal year 2008. The first was to correct a coding error for equipment purchased. The adjustment debited Office Equipment and Furniture-Under \$5,000 and credited Equipment over \$5,000 for \$23,071. The second entry was to record the May and June 2008 revenue in fiscal year 2008 instead of fiscal year 2009. Cash was debited and Miscellaneous General Revenue and Loan Related Revenues were credited for \$19,575 and \$3,486, respectively.

10. *Identify any disagreements with management, whether or not resolved to the auditor's satisfaction relating to a financial accounting, reporting, or auditing matter that could be significant to the financial statements.*

None.

11. *Identify any serious difficulties encountered in performing the audit.*

None.

12. *Identify any major issues discussed with management prior to retention.*

This is not applicable for audits conducted by the Office of the State Auditor.

*13. Identify any management consultations with other accountants about auditing and accounting matters.*

None.

*14. Identify any high-risk information technology systems critical to operations based on the auditor's overall assessment of the importance of the system to the agency and its mission, or whether any exceptions identified in the six audit report questions to be addressed by the auditors are directly related to the operations of an information technology system.*

ConnectND Finance, Human Resource Management System (HRMS), and Nortridge Loan System are high-risk information technology systems critical to the North Dakota Department of Veterans Affairs.

# ***Audit Objectives, Scope, and Methodology***

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## ***Audit Objectives***

The objectives of this audit of the North Dakota Department of Veterans Affairs for the two-year period ended June 30, 2008 were to provide reliable, audited financial statements and to answer the following questions:

1. What are the highest risk areas of the North Dakota Department of Veterans Affairs' operations and is internal control adequate in these areas?
2. What are the significant and high-risk areas of legislative intent applicable to the North Dakota Department of Veterans Affairs and are they in compliance with these laws?
3. Are there areas of the North Dakota Department of Veterans Affairs' operations where we can help to improve efficiency or effectiveness?

## ***Audit Scope***

This audit of the North Dakota Department of Veterans Affairs is for the two-year period ended June 30, 2008. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The North Dakota Department of Veterans Affairs' main office is in Fargo with a branch office in Bismarck, both offices were included in the audit scope.

## ***Audit Methodology***

To meet the objectives outlined above, we:

- Prepared financial statements from the legal balances on the state's accounting system tested as part of this audit and the audit of the state's Comprehensive Annual Financial Report and developed a discussion and analysis of the financial statements.
- Performed detailed analytical procedures including computer assisted auditing techniques. These procedures were used to identify high risk transactions and potential problem areas for additional testing.
- Tested internal control and compliance with laws and regulations which included selecting representative samples to determine if controls were operating effectively and to determine if laws were being followed consistently. Nonstatistical sampling was used and the results were projected to the population. Where applicable, populations were stratified to ensure that particular groups within a population were adequately represented in the sample, and to improve efficiency by gaining greater control on the composition of the sample.
- Interviewed appropriate agency personnel.

- Queried the ConnectND (PeopleSoft) system. Significant evidence was obtained from ConnectND.
- Observed North Dakota Department of Veterans Affairs' processes and procedures.

In aggregate there were no significant limitations or uncertainties related to our overall assessment of the sufficiency and appropriateness of audit evidence.

## ***Discussion and Analysis***

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The accompanying financial statements have been prepared to present the North Dakota Department of Veterans Affairs' revenues and expenditures on the legal (budget) basis. The accompanying financial statements are not intended to be presented in accordance with generally accepted accounting principles (GAAP).

For the two-year period June 30, 2008, operations of the North Dakota Department of Veterans Affairs were primarily supported by appropriations from the state's general fund. This is supplemented by federal funding and fees credited to the agency's operating fund.

### ***Financial Summary***

Revenues consisted primarily of interest and investment income and loan related revenue. These all remained fairly constant for the North Dakota Department of Veterans Affairs, increasing only slightly. Total revenues were \$153,798 for the year ended June 30, 2008 as compared to \$130,230 for the year ended June 30, 2007.

Total expenditures for the North Dakota Department of Veterans Affairs were \$784,719 for the year ended June 30, 2008 as compared to \$603,200 for the year ended June 30, 2007. The increase in total expenditures for the audited period reflects primarily grants, benefits, and claims (which also account for 43% of total expenditures in both years). All other expenditures remained fairly constant.

Payments for grants, benefits, and claims increased due to changes in policies for the amounts the agency pays for those services, as well as adding a denture grant and hearing aid grant.

### ***Analysis of Significant Changes in Operations***

There were no significant changes in operations.

### ***Analysis of Significant Variances Between Final Budgeted and Actual Expenditures***

There were no significant variances between final budgeted and actual amounts.

# Financial Statements

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## Statement of Revenues and Expenditures

| <b><u>Revenues and Other Sources:</u></b> | <b><u>June 30, 2008</u></b> | <b><u>June 30, 2007</u></b> |
|---|-----------------------------|-----------------------------|
| Miscellaneous General Revenue             | \$ 128,840                  | \$ 121,751                  |
| Loan Related Revenues                     | 14,249                      | 4,890                       |
| Interest and Investment Earnings          | 4,406                       | 6,299                       |
| Sale of Capital Assets                    | 7,000                       |                             |
| Prior Year Correction                     |                             | (1,200)                     |
| <b>Total Revenues and Other Sources</b>   | <b>\$ 154,495</b>           | <b>\$ 131,739</b>           |

| <b><u>Expenditures and Other Uses:</u></b> |                   |                   |
|--|-------------------|-------------------|
| Grants, Benefits, and Claims               | \$ 379,890        | \$ 216,149        |
| Salaries and Benefits                      | 275,866           | 254,354           |
| Travel                                     | 34,606            | 34,719            |
| Rentals/Leases - Building/Land             | 27,211            | 20,254            |
| Office Equipment & Furniture-Under \$5,000 | 25,660            | 2,887             |
| IT-Communications                          | 8,181             | 6,353             |
| Operating Fees and Services                | 5,735             | 920               |
| IT - Data Processing                       | 3,853             | 2,843             |
| Office Supplies                            | 3,610             | 4,992             |
| Rentals/Leases-Equipment & Other           | 2,957             | 3,447             |
| Postage                                    | 2,607             | 5,332             |
| IT Contractual Services and Repairs        | 2,500             | 2,500             |
| Professional Development                   | 2,365             | 3,446             |
| IT Equip under \$5,000                     | 2,164             | 6,863             |
| Food and Clothing                          | 1,563             |                   |
| Printing                                   | 1,540             | 2,076             |
| Building, Grounds, Vehicle Supply          | 1,179             | (40)              |
| Insurance                                  | 835               | 798               |
| Supply/Material-Professional               | 657               | 1,362             |
| Fees - Professional Services               | 1,238             | 4,812             |
| Repairs                                    | 536               | 426               |
| Supplies - IT Software                     | 369               | 6,171             |
| Miscellaneous Supplies                     | 155               | 5                 |
| Utilities                                  | 138               |                   |
| Other Equip under \$5,000                  |                   | 40                |
| Motor Vehicles                             |                   | 24,000            |
| <b>Total Expenditures and Other Uses</b>   | <b>\$ 785,417</b> | <b>\$ 604,709</b> |

## Statement of Appropriations

### For The Biennium Ended June 30, 2007

| Expenditures by<br>Line Item: | Original      |             | Expenditures |            | Unexpended<br>Appropriations |
|-------------------------------|---------------|-------------|--------------|------------|------------------------------|
|                               | Appropriation | Adjustments | FY 2006      | FY 2007    |                              |
| Vets Affairs Administration   | \$ 653,668    |             | \$ 309,633   | \$ 341,863 | \$ 2,172                     |
| Totals                        | \$ 653,668    |             | \$ 309,633   | \$ 341,863 | \$ 2,172                     |
| Expenditures by<br>Source:    |               |             |              |            |                              |
| General Fund                  | \$ 653,668    |             | \$ 309,633   | \$ 341,863 | \$ 2,172                     |
| Totals                        | \$ 653,668    |             | \$ 309,633   | \$ 341,863 | \$ 2,172                     |

### For The Year Ended June 30, 2008

| Expenditures by<br>Line Item: | Original      |             | Expenditures |  | Unexpended<br>Appropriations |
|-------------------------------|---------------|-------------|--------------|--|------------------------------|
|                               | Appropriation | Adjustments | FY2008       |  |                              |
| Vets Affairs Administration   | \$ 866,772    | \$ 11,506   | \$ 397,816   |  | \$ 480,462                   |
| Totals                        | \$ 866,772    | \$ 11,506   | \$ 397,816   |  | \$ 480,462                   |
| Expenditures by<br>Source:    |               |             |              |  |                              |
| General Fund                  | \$ 866,772    | \$ 11,506   | \$ 397,816   |  | \$ 480,462                   |
| Totals                        | \$ 866,772    | \$ 11,506   | \$ 397,816   |  | \$ 480,462                   |

#### Appropriation Adjustments:

The \$11,506 adjustment is for market equity compensation pursuant to Senate Bill 2189.

#### Expenditures Without Appropriations Of Specific Amounts:

The Veterans Post War Trust fund has a continuing appropriation authorized by NDCC 37-14-14 (fund 410). This fund had expenditures for fiscal year 2008 and fiscal year 2007 of \$195,780 and \$130,869, respectively.

## ***Internal Control***

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In our audit for the two-year period ended June 30, 2008, we identified the following areas of the North Dakota Department of Veterans Affairs' internal control as being the highest risk:

### ***Internal Controls Subjected to Testing:***

- Controls surrounding the processing of revenues.
- Controls surrounding the processing of expenditures.
- Controls effecting the safeguarding of assets.
- Controls relating to compliance with legislative intent.
- Controls surrounding the ConnectND (PeopleSoft) system.
- Controls surrounding the computer-based Nortridge Loan System.

The criteria used to evaluate internal control is published in the publication *Internal Control – Integrated Framework* from the Committee of Sponsoring Organizations (COSO) of the Treadway Commission.

We gained an understanding of internal control surrounding these areas and concluded as to the adequacy of their design. We also tested the operating effectiveness of those controls we considered necessary based on our assessment of audit risk. We concluded that internal control was not adequate noting a certain matter involving internal control and its operation that we consider to be a significant deficiency.

Auditors are required to report deficiencies in internal control that are significant within the context of the objectives of the audit. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect (1) misstatements in financial or performance information, (2) violations of laws and regulations, or (3) impairments of effectiveness or efficiency of operations, on a timely basis. Considering both qualitative and quantitative factors, we identified the following significant deficiency in internal control. We also noted other matters involving internal control that we have reported to management of the North Dakota Department of Veterans Affairs in a management letter dated July 7, 2009.

### ***Loan Receivables (Finding 08-1)***

We noted several problems with the Loans Receivable at June 30, 2008 and 2007:

- The trial balances run for June 30, 2008 and 2007 were not accurate. They included current loans entered into during fiscal year 2009 and loans that were previously written off. Each time the report was run a different ending balance was reported.
- The support for the Loans Receivable closing packages for fiscal year 2008 and 2007 was not maintained; therefore we were unable to tie out those balances. The trial balances we received did not agree to the closing packages submitted to OMB.
- We noted many receivable balances with an inconsequential amount left in the balance that is not going to be paid, but was still on the system.

**Recommendation:**

We recommend the North Dakota Department of Veterans Affairs:

- Run accurate reports of the loans receivable at year end and those reports be kept as support for the closing packages and
- Any inconsequential balance that is not deemed to be collected be written off to clean-up the system.

***North Dakota Department of Veterans Affairs' Response:***

*We agree. These recommendations will be implemented at the close of this year.*

## *Compliance With Legislative Intent*

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In our audit for the two-year period ended June 30, 2008, we identified and tested the North Dakota Department of Veterans Affairs' compliance with legislative intent for the following areas that we determined to be significant and of higher risk of noncompliance:

- The Veterans Aid Fund is used for the purpose of making loans, collecting loans, and paying administrative expense (North Dakota Century Code section 37-14-03.3).
- Loans are limited to \$5,000 with interest rates not exceeding 10% (NDCC 37-14-06, 07).
- The subcommittee of the North Dakota Department of Veterans Affairs conducted an annual performance evaluation of the commissioner and created and implemented a strategic plan (NDCC 37-18.1-03 part 5).
- Committee members are reimbursed for travel expenses and meals and lodging at the same rate as other state employees (NDCC 37-18.1-04).
- Proper use of the State Treasurer (State Constitution, article X, section 12).
- Compliance with appropriations and related transfers (2007 North Dakota Session Laws chapters 7 and 306).
- Compliance with OMB's Purchasing Procedures Manual.
- Travel-related expenditures are made in accordance with OMB policy and state statute (NDCC 44-08-04 and NDCC 54-06-09).
- Proper use of outside bank accounts and proper authority for investments outside the Bank of North Dakota (NDCC 6-09-07 and NDCC 21-04-02).
- Adequate blanket bond coverage of employees (NDCC 26.1-21-08).
- Compliance with fixed asset requirements including record keeping and surplus property (NDCC 54-27-21, NDCC 44-04-07 and NDCC 54-44-04 part 6).
- Compliance with payroll related laws including statutory salaries for applicable elected and appointed positions, and certification of payroll (NDCC 54-44.3-16).

The criteria used to evaluate legislative intent are the laws as published in the *North Dakota Century Code* and the *North Dakota Session Laws*.

*Government Auditing Standards* require auditors to report all instances of fraud and illegal acts unless they are inconsequential within the context of the audit objectives. Further, auditors are required to report significant violations of provisions of contracts or grant agreements, and significant abuse that has occurred or is likely to have occurred.

The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*. Thus, we concluded there was compliance with the legislative intent identified above.

## *Operations*

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This audit did not identify areas of the North Dakota Department of Veterans Affairs' operations where we determined it was practical at this time to help to improve efficiency or effectiveness.



STATE OF NORTH DAKOTA  
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600 E. BOULEVARD AVENUE - DEPT. 117  
BISMARCK, NORTH DAKOTA 58505

## ***Management Letter (Informal Recommendations)***

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July 7, 2009

Mr. Lonnie Wangen, Commissioner  
North Dakota Department of Veterans Affairs  
4201 38<sup>th</sup> Street SW, Suite 104  
Fargo, ND 58106-9003

Dear Mr. Wangen:

We have performed an audit of the North Dakota Department of Veterans Affairs for the two-year period ended June 30, 2008, and have issued a report thereon. As part of our audit, we gained an understanding of the North Dakota Department of Veterans Affairs' internal control structure to the extent we considered necessary to achieve our audit objectives. We also performed tests of compliance as described in the same report.

Our audit procedures are designed primarily to enable us to report on our objectives including those related to internal control and compliance with laws and regulations and may not bring to light all weaknesses in systems and procedures or noncompliance with laws and regulations which may exist. We aim, however, to use our knowledge of your organization gained during our work to make comments and suggestions which we hope will be useful to you.

In connection with the audit, gaining an understanding of the internal control structure, and tests of compliance with laws and regulations referred to above, we noted certain conditions we did not consider reportable within the context of your audit report. These conditions relate to areas of general business practice or control issues that have no significant bearing on the administration of state or federal funds. We do, however, want to present our recommendations to you for your consideration and whatever follow-up action you consider appropriate. During the next audit we will determine if these recommendations have been implemented, and if not, we will reconsider their status.

The following present our informal recommendations.

## CODE OF ETHICS

### **Informal Recommendation 08-1:**

The North Dakota Department of Veterans Affairs has not adopted a code of ethics or code of business conduct.

Management should encourage honest and ethical conduct, including the ethical handling of actual or apparent conflicts of interest between person and professional relationships.

We recommend the North Dakota Department of Veterans Affairs adopt a code of ethics or code of business conduct. At a minimum, the following issues should be addressed:

1. Honest and ethical conduct;
2. Full, fair, accurate, timely, and understandable disclosure in reports and documents;
3. Compliance with applicable laws;
4. The prompt internal reporting of violations of the code;
5. Description of what constitutes fraudulent behavior; and
6. Accountability for adherence to the code and consequences for breaching it.

### **North Dakota Department of Veterans Affairs' Response:**

*We agree. We are working to adopt and implement a code of ethics.*

## REVENUES

### **Informal Recommendation 08-2:**

May and June 2008 revenue totaling \$23,000 for interest and principal was not recorded in fiscal year 2008, but was instead recorded in fiscal year 2009. These amounts should have been applied back to fiscal year 2008.

OMB policy 200 states every agency is required to identify and record receivables and other financial statement data at the close of each fiscal year. The financial data must be reported in accordance with generally accepted accounting principles relating to year-end accruals of receipts. The accounting system allows transactions to be applied to the previous month.

Informal Recommendation 08-2: We recommend that Veterans Affairs record revenues in the proper fiscal year and in a timely manner.

### **North Dakota Department of Veterans Affairs' Response:**

*We agree. This recommendation will be integrated into our future recordings in accordance with generally accepted accounting principles.*

## CONTROL/FRAUD RISK ASSESSMENT

### **Informal Recommendation 08-3:**

The Department of Veterans Affairs does not have a system in place to identify control weaknesses and possible instances of fraud or fraudulent activities in the Department of Veterans Affairs' financial and operational areas. This would include the documentation of the necessary control activities to ensure significant control weaknesses (including fraud exposure) are identified and mitigated.

The most important guidance relating to internal control is contained in *Internal Control – Integrated Framework* published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). This guidance dictates that a Control Risk Assessment including a Fraud Risk Assessment program be established and practiced to identify risks within the department's control environment including fraudulent type activities, when special circumstances arise, when changing operating environments, and for restructuring.

We recommend that the North Dakota Department of Veterans Affairs, with the assistance of the Office of Management and Budget:

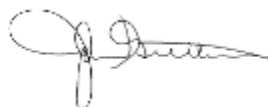
- Establish and perform a control risk assessment including a fraud risk assessment on a recurring basis; and
- Design and document the necessary control activities to ensure that each of the significant control risks and fraud exposures identified during the risk assessment process has been adequately mitigated.

### **North Dakota Department of Veterans Affairs' Response:**

*We agree. This department will establish a control/fraud risk assessment and maintain documentation.*

I encourage you to call myself at 239-7289 if you have any questions about the implementation of recommendations included in your audit report or this letter.

Sincerely,



John Grettum, CPA  
Audit Manager, Division of State Audit

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