

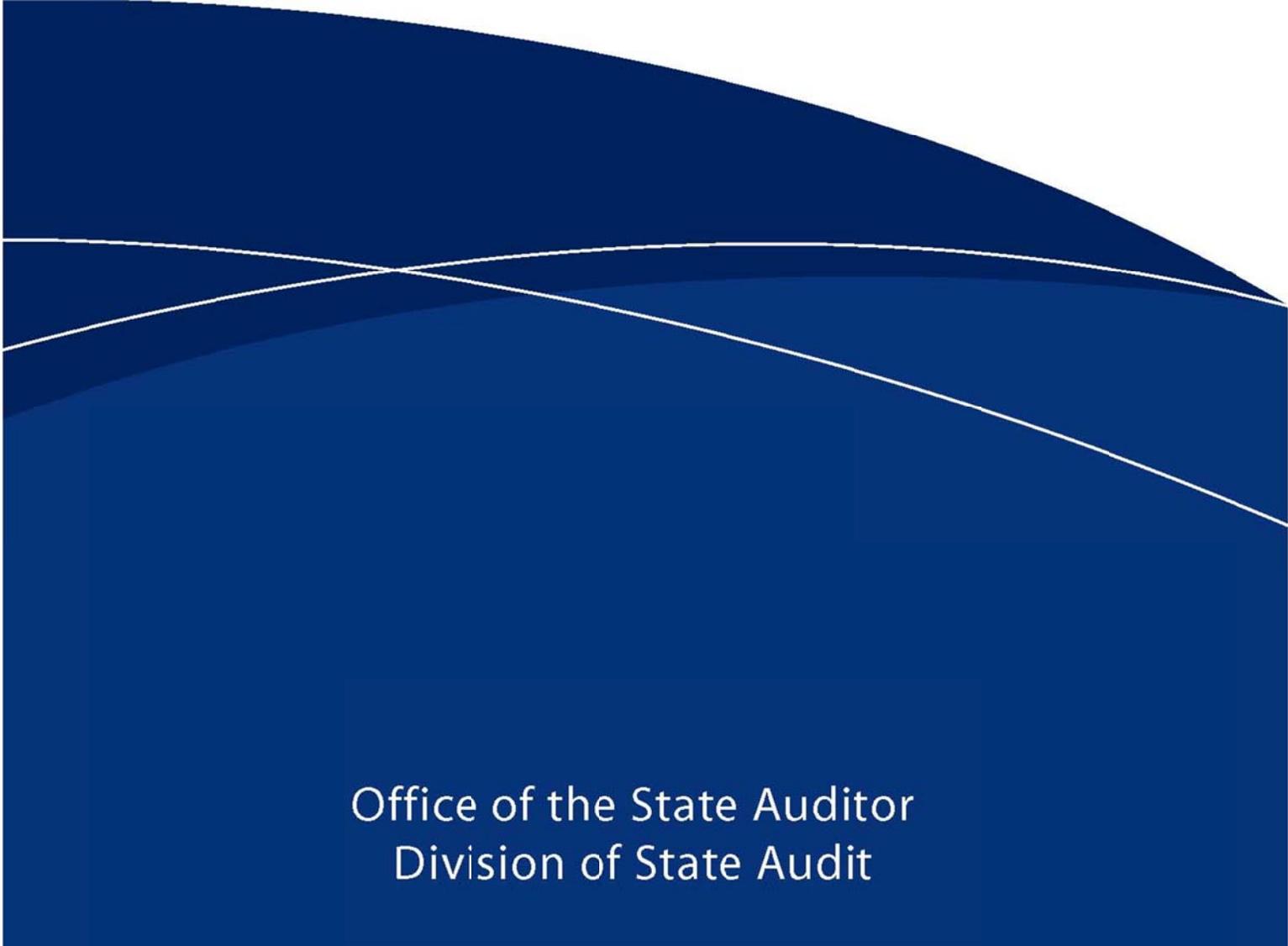


DEPARTMENT OF
AGRICULTURE
BISMARCK, NORTH DAKOTA

Audit Report

For the Biennium Ended
June 30, 2009

ROBERT R. PETERSON
STATE AUDITOR



Office of the State Auditor
Division of State Audit

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Transmittal Letter

March 30, 2010

The Honorable John Hoeven, Governor
Members of the North Dakota Legislative Assembly
The Honorable Doug Goehring, Agriculture Commissioner

We are pleased to submit this audit of the Department of Agriculture for the biennium ended June 30, 2009. 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 Kevin Scherbenske, CPA. Sarah Kuntz was the staff auditor. Fred Ehrhardt, CPA was the audit supervisor. Inquiries or comments relating to this audit may be directed to the audit supervisor by calling (701) 328-2241. We wish to express our appreciation to Commissioner Goehring 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

Introduction

The North Dakota Department of Agriculture was originally established as the Commissioner of Agriculture and Labor by the North Dakota Constitution in 1889. In 1964, voters approved dividing the office into two separate offices – Commissioner of Labor and Commissioner of Agriculture.

The responsibilities of the Department of Agriculture include: a leadership role in the formulation of policies affecting the state's agricultural industries; the advocacy of the needs and concerns of farmers and ranchers at the state and national level; the administration of fair and timely mediation services to farmers and ranchers; the promotion and marketing of North Dakota products; and the dissemination of information concerning agricultural issues to the Governor.

Responses to LAFRC Audit Questions

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

Financial statements were not prepared by the Department of Agriculture 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 "Fraud Risk Assessment" as noted on page 11, 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 North Dakota Department of Agriculture did not implement the recommendation included in the prior audit report addressing "Fraud Risk Assessment" as noted on page 16.

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 17 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 Department of Agriculture's financial statements do not include any significant accounting estimates.

9. *Identify any significant audit adjustments.*

Significant audit adjustments were not necessary.

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 and Human Resource Management System (HRMS) are high-risk information technology systems critical to the Department of Agriculture.

Audit Objectives, Scope, and Methodology

Audit Objectives

The objectives of this audit of the Department of Agriculture for the biennium ended June 30, 2009 were to provide reliable, audited financial statements and to answer the following questions:

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

Audit Scope

This audit of the Department of Agriculture is for the biennium ended June 30, 2009. 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 the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The Department of Agriculture's sole location is its Bismarck office, which was 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 reviewed management's 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. Non-statistical 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 Department of Agriculture's 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.

Management's Discussion and Analysis

The accompanying financial statements have been prepared to present the Department of Agriculture's 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).

The following management discussion and analysis was prepared by the Department of Agriculture's management. We have applied certain limited procedures, which consisted primarily of inquiries of management regarding the methods of measurement and presentation of this supplementary information to ensure it does not conflict with the knowledge we gained as part of our audit.

For the biennium ended June 30, 2009, operations of the Department of Agriculture were primarily supported by federal funding and fees credited to the agency's operating fund. This is supplemented by appropriations from the state's general fund.

Financial Summary

Revenues consisted primarily of federal funds from a variety of federal grants and other revenues derived mainly from licenses, registrations, interagency transfers, and user fees. Total revenues and other sources were \$5,406,781 for the year ended June 30, 2009 as compared to \$8,432,103 for the year ended June 30, 2008. This decrease is due to pesticide registrations on a two-year cycle with registrations due the first year of the biennium.

Total expenditures and other uses for the Department of Agriculture were \$9,021,963 for the year ended June 30, 2009, as compared to \$7,380,880 for the prior year. The increase in total expenditures for the audited period reflects primarily grants to individuals for the Livestock Feed Transportation program for \$1,000,000, as well as an increase in federal expenditures for the livestock pollution prevention program. All other expenditures remained fairly constant.

The increase in expenditures for salaries and benefits reflected the general salary increases.

Analysis of Significant Changes in Operations

The Department of Agriculture implemented a number of significant changes during the 2007-2009 biennium.

In 2008, the Department of Agriculture prepared and submitted to the Environmental Protection Agency (EPA) a proposed endangered species protection program for pesticides that established a framework for the Department to submit data and recommendations to enhance the protection of North Dakota's listed species from pesticides.

The Department also coordinated an extensive pesticide surface water monitoring program, assessing levels of 186 different pesticides in three different watersheds in the state. The Department also expanded its Water Quality Advisory Committee to develop its list of "Pesticides of Interest" and reduced that list to the list of "Pesticides of Concern."

Consistent with a renewed focus on risk-based pesticide regulation and compliance assistance, the Department diverted regulatory activities away from lower-risk activities such as record-keeping and bulk repackaging to activities, such as use inspections, where we were best positioned to educate pesticide users. This focus resulted in a 50% decrease in the number of enforcement actions from 340 in 2007 to 169 in 2008. In 2009, the Department issued a total of 168 enforcement actions, including 120 warnings and 48 civil penalties. This trend in enforcement actions indicated the Department's new focus on compliance assistance and communication improved overall compliance with state and federal pesticide regulations.

The Department also made great strides in working with local, state, and federal officials on noxious weed control issues. On March 3, 2009, the Department held a public hearing to discuss the control of noxious weeds on the eastern shore of Lake Oahe. Years of drought, low water levels, and dwindling federal agency budgets resulted in public frustration regarding the spread of noxious weeds on public lands surrounding the Oahe Reservoir.

The Department also developed a program to certify weed seed-free forage. Due to the growing demand for weed seed-free forage, the Department developed a training program to certify forage inspectors.

The Department received federal grants to enhance the competitiveness of specialty crops. Specialty crops now grown commercially in North Dakota include dry beans, dry peas, lentils, potatoes, grapes, honey, and various vegetables. Over \$200,000 was distributed to enhance research, promotion, marketing, trade enhancement, education, and product development.

Livestock producers suffered significant losses during the harsh 2008-2009 winter. Producers who incurred extraordinary feed-related expenses or losses were provided compensation through the 2009 Livestock Feed Transportation Program. Funding for the program included a \$750,000 United States Department of Agriculture grant with an additional \$250,000 state funding provided by the North Dakota Legislature.

Financial Statements

Statement of Revenues and Expenditures

	<u>June 30, 2009</u>	<u>June 30, 2008</u>
<u>Revenues and Other Sources:</u>		
Federal Revenue	\$2,525,367	\$1,882,569
Pesticide Registration	366,250	3,709,825
Fertilizer Registration	383,316	547,906
Commercial Feed Registration and Tonnage	223,674	693,874
Conference Registration Fees	171,992	169,209
Other Licenses, Permits, and Fees	90,104	112,758
Apiary Licenses	84,885	78,702
Inspection Fees	45,039	46,121
Turkey Assessments	18,781	25,368
Fines and Forfeits	15,292	39,743
Miscellaneous Revenue	13,609	14,173
Transfers In	1,468,472	1,111,855
Total Revenues and Other Sources	<u>\$5,406,781</u>	<u>\$8,432,103</u>
<u>Expenditures and Other Uses:</u>		
Salaries and Benefits	\$3,954,710	\$3,679,457
Grants:		
Individuals	1,000,000	
Counties	564,777	590,447
Associations/State Colleges	139,399	113,375
Operating Fees	586,336	505,787
Wildlife Services	583,894	495,106
Travel	517,388	512,620
Livestock Pollution Prevention	464,099	195,588
IT – Equip/Data Processing/Software/Repairs	302,013	253,405
Project Safe Send	235,193	210,904
Supplies/Postage	152,953	146,779
Rent of Building Space	90,224	80,487
Professional Development	84,951	100,594
Veterinarian Fees/Supplies	61,289	92,297
Printing	55,759	40,001
Other Expenditures	140,890	95,381
Transfers Out	88,088	268,652
Total Expenditures and Other Uses	<u>\$9,021,963</u>	<u>\$7,380,880</u>

Statement of Appropriations

For The Biennium Ended June 30, 2009

Expenditures by Line Item:	<u>Original Appropriation</u>	<u>Adjustments</u>	<u>Final Appropriation</u>	<u>Expenditures</u>	<u>Unexpended Appropriation</u>
Salaries and Benefits	\$ 6,984,840	\$ 189,109	\$ 7,173,949	\$ 6,500,292	\$ 673,657
Operating Expenses	4,714,383	241,658	4,956,041	4,000,246	955,795
Capital Assets	5,000	10,700	15,700	11,878	3,822
Grants	1,849,225	1,000,000	2,849,225	2,386,576	462,649
Board of Animal Health	2,390,538	(3,270)	2,387,268	1,815,254	572,014
Wildlife Services	1,209,000	(130,000)	1,079,000	1,079,000	
Crop Harmonization Board	25,000		25,000	23,811	1,189
Totals	<u>\$ 17,117,986</u>	<u>\$ 1,308,197</u>	<u>\$ 18,486,183</u>	<u>\$ 15,817,056</u>	<u>\$ 2,669,127</u>
Expenditures by Source:					
General Fund	\$ 5,789,660	\$ 27,007	\$ 5,816,667	\$ 5,797,657	\$ 19,010
Other Funds	11,388,326	1,281,190	12,669,516	10,019,399	2,650,117
Totals	<u>\$ 17,177,986</u>	<u>\$ 1,308,197</u>	<u>\$ 18,486,183</u>	<u>\$ 15,817,056</u>	<u>\$ 2,669,127</u>

Appropriation Adjustments:

\$56,277 of the adjustment to the Salaries and Wages line was due to additional appropriation authority granted by Senate Bill 2189 of the 2007 session for market equity increases for classified state employees.

The remaining \$132,832 increase in the Salaries and Wages line as well as \$131,533 of the increase in the Operating Expenses line was due to additional authority received to conduct a potato cyst nematode survey and was approved by the Emergency Commission.

The remaining \$120,825 increase in the Operating Expense line was due to additional authority received for Pride of Dakota showcases and was approved by the Emergency Commission.

\$10,700 was moved from the Operating Expense line to the Capital Assets line for the purchase of a new copier and was approved by the Emergency Commission.

The \$1,000,000 increase in the Grants line was due to additional authority received to assist livestock producers affected by the 2009 spring flood and was approved by the Emergency Commission.

The \$3,270 reduction in the Board of Animal Health line and \$130,000 reduction in the Wildlife Services line are due to reduce the amount available in the 2007-2009 biennium for funds spent in the prior biennium under an emergency measure.

Expenditures Without Appropriations Of Specific Amounts:

Pesticide civil penalties authorized by NDCC section 4-35-28 (\$54,193 of expenditures for this biennium).

The Statewide Conference Fund is nonappropriated in accordance with OMB policy 211 (\$31,088 of expenditures for this biennium).

Turkey Promotion Fund has a continuing appropriation authorized by NDCC section 4-13.1-05 (\$49,394 of expenditures for this biennium).

Honey Promotion Fund has a continuing appropriation authorized by NDCC section 4-12.1-03 (\$25,120 of expenditures for this biennium).

Minor Use Pesticide Fund has a continuing appropriation authorized by NDCC section 4-35-06.3 (\$128,910 of expenditures for this biennium).

Anhydrous Ammonia Storage Inspection Fund expenditures where authorized by Senate Bill 2010, section 10 of the 2007 Session Laws (\$97,079 of expenditures for this biennium).

Environment and Rangeland Protection Fund expenditures where authorized by Senate Bill 2009, section 11 of the 2007 Session Laws (\$200,000 of expenditures for this biennium).

Internal Control

In our audit for the biennium ended June 30, 2009, we identified the following areas of the Department of Agriculture's 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 relating to compliance with legislative intent.
- Controls surrounding the ConnectND (PeopleSoft) 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 the management of the North Dakota Department of Agriculture in a management letter dated March 30, 2010.

Fraud Risk Assessment (Finding 09-1)

The Department of Agriculture does not have a system in place to identify possible instances of fraud or fraudulent activities in the agency's financial and operational areas.

The most important guidance relating to internal control is contained in *Internal Control – Integrated Framework* published by the Committee of Sponsoring Organizations of Treadway Commission (COSO). This guidance dictates a Fraud Risk Assessment program be established and practiced to identify risks of fraudulent type activities including when special circumstances arise, when changing operating environments, and for restructuring. In addition, the Department of Agriculture does not have the necessary control activities designed/documented to ensure significant fraud exposures are identified and mitigated.

Recommendation:

We recommend the Department of Agriculture:

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

Department of Agriculture Response:

We agree that this recommendation may reduce future fraud in state agencies. We will establish and perform a fraud risk assessment, and we will design and document the resulting control activities from the risk assessment.

Compliance With Legislative Intent

In our audit for the biennium ended June 30, 2009, we identified and tested the Department of Agriculture's compliance with legislative intent for the following areas we determined to be significant and of higher risk of noncompliance:

- Limited use of funds from the Environment and Rangeland Protection Fund to \$3,142,109 (2007 North Dakota Session Laws chapter 36, section 4).
- Limited use of funds from the Anhydrous Ammonia Storage Inspection Fund to \$65,912 (2007 North Dakota Session Laws chapter 36, section 5).
- Limited use of funds from the Game and Fish Department to \$1,019,684 (2007 North Dakota Session Laws chapter 36, section 6).
- Proper transfer of \$150,000 from the General Fund to the Environment and Rangeland Protection Fund (2007 North Dakota Session Laws chapter 36, section 8).
- Proper transfer of \$50,000 from the Pesticide Enforcement Fund to the Environment and Rangeland Protection Fund (2007 North Dakota Session Laws chapter 36, section 9).
- Proper transfer of \$200,000 from the Environment and Rangeland Protection Fund to the Minor Use Pesticide Fund (2007 North Dakota Session Laws chapter 36, section 11).
- Report on the use of funding for an animal tracking data base (2007 North Dakota Session Laws chapter 36, section 12).
- Limited use of funds from the Environment and Rangeland Protection Fund and Oilseed Fund to \$79,500 each for blackbird mitigation (2007 North Dakota Session Laws chapter 52, section 1).
- Brucellosis and identification tags cost (NDCC 36-01-08).
- Reporting to legislative committees on the status of the pesticide container disposal program (NDCC 4-35.2-03).
- Proper use of the following legally restricted funds:
 - Turkey Fund (NDCC 4-13.1-05).
 - Honey Promotion Fund (NDCC 4-12.1-03).
 - State Waterbank Fund (NDCC 61-31-10).
 - Minor Use Pesticide Fund (NDCC 4-35-06.3).
 - Anhydrous Ammonia Storage Inspection Fund (NDCC 19-20.2-08.1).
 - Environment and Rangeland Protection Fund (NDCC 19-18-02.1).
- Application of proper statutory rates relating to revenue.
- Adequate blanket bond coverage of employees (NDCC section 26.1-21-08).
- Compliance with appropriations (2007 North Dakota Session Laws chapter 36).

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

This audit did not identify areas of the Department of Agriculture's operations where we determined it was practical at this time to help to improve efficiency or effectiveness. However, we did note a certain matter involving operations that we have reported to the management of the Department of Agriculture in a management letter dated March 30, 2010.

Prior Recommendations Not Implemented

Prior recommendations have been implemented with the exception of the following:

Fraud Risk Assessment (Finding 07-1)

Recommendation:

We recommend the North Dakota Department of Agriculture:

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

Status: Not implemented – see page 11.



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

Management Letter (Informal Recommendations)

March 30, 2010

The Honorable Doug Goehring
Agriculture Commissioner
Department of Agriculture
600 E. Boulevard Avenue
Bismarck, ND 58505

Dear Commissioner Goehring:

We have performed an audit of the Department of Agriculture for the biennium ended June 30, 2009, and have issued a report thereon. As part of our audit, we gained an understanding of the Department of Agriculture's 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 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.

CASH

Informal Recommendation 09-1: We recommend the Department of Agriculture have someone independent of drawing down federal funds perform a reconciliation of federal funds recorded on PeopleSoft to the amount shown by the federal government as paid to the agency.

GENERAL

Informal Recommendation 09-2: We recommend the Department of Agriculture develop a code of ethics and code of business conduct and ensure that employees adhere to the policy.

EXPENDITURES

Informal Recommendation 09-3: We recommend the Department of Agriculture look for ways to increase their usage of the P-card as a form of payment. We further recommend, if necessary, they meet with officials from OMB to facilitate this process by raising P-card limits, determining which of their vendors they could be making P-card payments to, or changing the accounting on their P-cards so as to limit or eliminate the need to re-allocate P-card expenditures.

Management of Department of Agriculture agreed with these recommendations.

I encourage you to call myself or an audit manager at 328-2241 if you have any questions about the implementation of recommendations included in your audit report or this letter.

Sincerely,



Kevin Scherbenske
Auditor in-charge

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