

Office of the State Auditor

Division of State Audit

North Dakota State Seed Department Fargo, North Dakota

Audit Report for the
Two Year Period Ended June 30, 2008
Client Code 61600

Robert R. Peterson
State Auditor



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STATE OF NORTH DAKOTA
OFFICE OF THE STATE AUDITOR
STATE CAPITOL
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BISMARCK, NORTH DAKOTA 58505

Transmittal Letter

May 20, 2009

The Honorable John Hoeven, Governor
Members of the North Dakota Legislative Assembly
Ken Bertsch, State Seed Commissioner, North Dakota State Seed Department
Members of the North Dakota State Seed Commission

We are pleased to submit this audit of the North Dakota State Seed Department 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 Dave Feltman. Robyn Hoffmann, CPA and Mary Feltman, CPA were the staff auditors. 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 Bertsch 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 Legislature established the North Dakota State Seed Department in 1931. The Department was designated as a separate agency of government to be located on the campus of the North Dakota State University in Fargo, acting as the official seed certification agency for the state. A nine-member seed commission acts as board of directors for the agency. Members are selected to serve by various agriculture industry organizations, including the North Dakota Crop Improvement Association, the North Dakota Certified Seed Potato Growers Association, the North Dakota Agricultural Association, the Northern Plains Potato Growers Association, the North Dakota Potato Council, the North Dakota Grain Dealers Association, the North Dakota Dry Edible Bean Seed Growers Association and the Director of the North Dakota State University Agriculture Experiment Station. The Commissioner of Agriculture, or his designee, serves as chairman of the Commission. The Commission appoints a State Seed Commissioner, who serves as chief executive officer of the Department.

RESPONSES TO LAFRC AUDIT QUESTIONS

The Legislative Audit and Fiscal Review Committee (LAFRC) requests that certain items be addressed by auditors performing audits of state agencies.

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

Financial statements were not prepared by the North Dakota State Seed Department 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 "control/fraud risk assessment" (page10), 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?*

Yes, the North Dakota State Seed Department has implemented the recommendation 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.*

No, a management letter was not issued.

LAFRC AUDIT COMMUNICATIONS

1. *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.

2. *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.*

None

3. *Identify any significant audit adjustments.*

None

4. *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

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

None

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

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

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

None

8. *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 State Seed Administration Software (SSAS) are high-risk information technology systems critical to the North Dakota State Seed Department. The exception noted was not directly related to the operations of an information technology system.

Audit Objectives, Scope, And Methodology

Audit Objectives

The objectives of this audit of the North Dakota State Seed Department 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 State Seed Department'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 North Dakota State Seed Department and are they in compliance with these laws?
3. Are there areas of the North Dakota State Seed Department's operations where we can help to improve efficiency or effectiveness?

Audit Scope

This audit of the North Dakota State Seed Department 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 State Seed Department has operations in the following locations. Each location will be included in the audit scope:

- The central office in Fargo.
- A branch office in Grafton.

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. Further 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) ERP system. Given the complexity of the State's accounting system significant evidence was obtained from ConnectND.
- Observed North Dakota State Seed Department'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.

Confidential or Sensitive
Information Omitted

None.

Discussion And Analysis

The accompanying financial statements have been prepared to present the North Dakota State Seed Department'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).

For the two-year period ended June 30, 2008, operations of the North Dakota State Seed Department were primarily supported by fees for services they provide to the agricultural industry.

FINANCIAL SUMMARY

Revenues consisted primarily of regulatory fees. Other revenues during the audited period included earnings from interest on investments and fees for services. These revenues all remained fairly constant, except for fees for services, which increased due to new seed varieties subject to royalty assessment. Total revenues were \$2,657,553 for the year ended June 30, 2008 as compared to \$2,493,241 for the year ended June 30, 2007.

Total expenditures also remained fairly constant for the North Dakota State Seed Department, except for grants, benefits and claims; which increased due to a grant of \$250,000 to the North Dakota State University Agricultural Experiment Station for a new greenhouse facility. Expenditures were \$2,402,130 for the year ended June 30, 2008 as compared to \$2,098,890 for the prior year. Payments for salaries and benefits accounted for approximately 69% of the expenditures.

ANALYSIS OF SIGNIFICANT CHANGES IN OPERATIONS

There were no significant changes in operation.

ANALYSIS OF SIGNIFICANT VARIANCES BETWEEN FINAL BUDGETED AND ACTUAL EXPENDITURES

For the fiscal years ended June 30, 2008 and 2007, there were no significant variances between the original and final budgeted amounts or between the final budgeted and actual expenditures.

Financial Statements

STATEMENT OF REVENUES AND EXPENDITURES

Revenues and Other Sources:	June 30, 2008	June 30, 2007
Regulatory Fees	\$ 2,457,607	\$ 2,322,124
Interest & Investment Earnings	95,965	93,384
Fees for Services	95,283	64,978
Licenses, Permits & Fees	7,670	6,073
Miscellaneous General Revenue	1,028	982
Intergovernmental Grants/Contracts		5,700
Total Revenues and Other Sources	\$ 2,657,553	\$ 2,493,241
Expenditures and Other Uses:		
Salaries and Benefits	\$ 1,581,830	\$ 1,505,872
Grants, Benefits & Claims	300,000	50,000
Travel	150,602	164,676
Utilities	74,266	68,419
Operating Fees and Services	36,584	29,321
Lab Supplies	35,694	20,816
Professional Development	30,344	30,375
Postage	29,366	23,581
Supply/Material-Professional	23,038	30,492
Fees - Professional Services	22,394	16,365
Printing	19,983	25,875
IT Contractual Services and Repairs	19,084	16,679
IT-Communications	14,553	13,688
Repairs	12,564	20,075
Rentals/Leases-Equip & Other	11,909	12,272
Office Supplies	11,006	22,971
IT Equipment Over \$5000	10,341	0
Supplies - IT Software	7,074	6,414
IT - Data Processing	6,783	6,256
Miscellaneous Supplies	1,819	15,577
Insurance	1,627	5,167
Bldg, Grounds, Vehicle Supply	1,269	1,477
Other Equip under \$5,000	0	5,205
Equipment Over \$5000	0	7,317
Total Expenses and Other Uses	\$ 2,402,130	\$ 2,098,890

STATEMENT OF APPROPRIATIONS

For The Biennium Ended June 30, 2007

	Original Appropriation	Adjustments	Final Appropriation	Total Expenditures	Unexpended Appropriation
Contingencies	\$ 5,933,391		\$ 5,933,391	\$ 4,125,737	\$ 1,807,654
Totals	\$ 5,933,391	\$ -	\$ 5,933,391	\$ 4,125,737	\$ 1,807,654
Expenditures by Source:					
Other Funds	\$ 5,933,391		\$ 5,933,391	\$ 4,125,737	\$ 1,807,654
Totals	\$ 5,933,391	\$ -	\$ 5,933,391	\$ 4,125,737	\$ 1,807,654

For The Year Ended June 30, 2008

	Original Appropriation	Adjustments	Adjusted Appropriation	FY 2008 Expenditures	Unexpended Appropriation
Seed Operations	\$ 6,166,218	\$ 12,908	\$ 6,179,126	\$ 2,402,130	\$ 3,776,996
Totals	\$ 6,166,218	\$ 12,908	\$ 6,179,126	\$ 2,402,130	\$ 3,776,996
Expenditures by Source:					
Other Funds	\$ 6,166,218	\$ 12,908	\$ 6,179,126	\$ 2,402,130	\$ 3,776,996
Totals	\$ 6,166,218	\$ 12,908	\$ 6,179,126	\$ 2,402,130	\$ 3,776,996

Appropriation Adjustments:

Market equity compensation adjustment pursuant to SB 2189.

Internal Control

In our audit for the two-year period ended June 30, 2008, we identified the following areas of the North Dakota State Seed Department'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 effecting the safeguarding of assets.
- Controls relating to compliance with legislative intent.
- Controls surrounding the ConnectND (PeopleSoft) system.
- Controls surrounding the computer-based financial administrative software.

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.

Finding 08-1

CONTROL/FRAUD RISK ASSESSMENT

The North Dakota State Seed Department does not have a system in place to identify control weaknesses and possible instances of fraud or fraudulent activities in the department's 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.

Audit Recommendation
and Agency Response

Recommendation:

We recommend the North Dakota State Seed Department

- 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 State Seed Department Response:

North Dakota State Seed acknowledges the recommendation regarding fraud risk assessment and internal controls. NDSSD received the OMB Risk Assessment template immediately prior to our biennial audit. We intend to utilize the template to construct a formal risk assessment model that fits agency operations in order to comply with the audit recommendation.

Compliance With Legislative Intent

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

Legislative Intent Included In Our Audit Scope

- Members of the Seed Commission are reimbursed \$75 per day and expenses as specified in NDCC 4-09-03.
- Seed Commission appointed a Commissioner and fixed his salary within legislative appropriation. (NDCC 4-09-03)
- Commissioner, with the approval of the Seed Commission, established and charged fees for laboratory tests and services. (NDCC 04-09-08).
- Rules and requirements for certification of crop seeds and for seed potato certifications were published in the department bulletin. (NDCC 4-09-18).
- Fees for making commodity grade inspections were determined by the Commissioner, with approval of the Seed Commission and are uniform throughout the state for specified periods of time. (NDCC 4-09.1-03).
- Nonresidents are required to submit an annual application for a nonresident seed dealer license and submit an annual license fee. (NDCC 4-25-04).
- Proper use of the State Treasurer (State Constitution, article X, section 12).
- Compliance with appropriations and related transfers (North Dakota Session Laws).
- Compliance with OMB's Purchasing Procedures Manual.
- Travel-related expenditures are made in accordance with OMB policy and state statute.
- Proper use of outside bank accounts, petty cash funds and proper authority for investments outside the Bank of North Dakota (NDCC 4-09-20, 6-09-07, 21-04-02, 54-06-08.1, and 54-27-16).
- Adequate blanket bond coverage of employees (NDCC section 26.1-21-08).
- Compliance with fixed asset requirements including record keeping, surplus property, lease and financing arrangements in budget requests, and lease analysis requirements.
- Compliance with payroll related laws including statutory salaries for applicable elected and appointed positions, and certification of payroll.

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 requires 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 have occurred or are 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 North Dakota State Seed Department's operations where we determined it was practical at this time to help to improve efficiency or effectiveness.
