

Department of Corrections
and Rehabilitation
BISMARCK, NORTH DAKOTA

Audit Report

For the Biennium Ended
June 30, 2011

ROBERT R. PETERSON
STATE AUDITOR

Office of the State Auditor
Division of State Audit

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OFFICE OF THE STATE AUDITOR
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Transmittal Letter

March 27, 2012

The Honorable Jack Dalrymple, Governor
Members of the North Dakota Legislative Assembly
Ms. Leann Bertsch, Director, Department of Corrections and Rehabilitation

We are pleased to submit this audit of the Department of Corrections and Rehabilitation for the biennium ended June 30, 2011. 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. Crystal Hoggarth and Sarah Kuntz were the staff auditors. Cindi Pedersen, CPA, was the audit manager. Inquiries or comments relating to this audit may be directed to the audit manager by calling (701) 328-2241. We wish to express our appreciation to Director Bertsch and her staff for the courtesy, cooperation, and assistance they provided to us during this audit.

Respectfully submitted,

A handwritten signature in black ink that reads "Bob Peterson".

Robert R. Peterson
State Auditor

Executive Summary

Introduction

The North Dakota Department of Corrections and Rehabilitation's mission is to protect the public while providing a safe and humane environment for both adults and juveniles placed in the Department's care and custody. The Department carries out the judgments of the North Dakota courts and provides rehabilitation programs in an effort to successfully reintegrate offenders back into society.

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 responses 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 Department of Corrections and Rehabilitation 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?

Other than our findings addressing "Sales to Inappropriate Vendors" (page 16) and "Improper Use of Public Funds" (page 17), the Department of Corrections and Rehabilitation was in compliance with significant statutes, laws, rules, and regulations under which it was created and is functioning.

3. Was internal control adequate and functioning effectively?

Other than our findings addressing the "Lack of Controls Over Pharmacy Inventory" (page 11) and "Control Weaknesses at Roughrider Industries" (page 13), 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.

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 20 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 Correction and Rehabilitation'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, Human Resource Management System (HRMS), Macola, and the Department of Corrections Subject Tracking and Reporting System (DOCSTARS) are high-risk information technology systems critical to the Department of Corrections and Rehabilitation.

Audit Objectives, Scope, and Methodology

Audit Objectives

The objectives of this audit of the Department of Corrections and Rehabilitation for the biennium ended June 30, 2011 were to provide reliable, audited financial statements and to answer the following questions:

1. What are the highest risk areas of the Department of Corrections and Rehabilitation'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 Corrections and Rehabilitation and are they in compliance with these laws?
3. Are there areas of the Department of Corrections and Rehabilitation's operations where we can help to improve efficiency or effectiveness?

Audit Scope

This audit of the Department of Corrections and Rehabilitation is for the biennium ended June 30, 2011. 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 Department of Corrections and Rehabilitation has operations in the following locations. Each location was included in the audit scope:

- North Dakota State Penitentiary
- James River Correctional Center
- Missouri River Correctional Center
- Youth Correctional Center

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 Corrections and Rehabilitation'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 Correction and Rehabilitation'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 Correction and Rehabilitation'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, 2011, operations of the Department of Corrections and Rehabilitation 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

The Department of Corrections and Rehabilitation revenues primarily consist of Roughrider Industries (RRI) sales, correctional fees collected from individuals on a parole and/or probation (supervision fees), transfers from the common schools trust fund, and federal funds. Total revenues increased approximately 20% in fiscal year 2011 compared to fiscal year 2010. The majority of the increase in the revenue from 2010 to 2011 is attributable to RRI sales. Over this period of time RRI sales increased by 48%. The major factor behind this significant increase is believed to be the strong North Dakota economy. Federal revenue increased by 9% from 2010 to 2011 primarily due to the receipt of funds appropriated through American Recovery and Reinvestment Act. Supervision fee revenue was stable. However, it is anticipated that future revenues from correctional fees will increase as the number of individuals under supervision in the community is currently increasing.

Total expenditures for the Department of Corrections and Rehabilitation increased 19% from fiscal year 2010 to fiscal year 2011. The majority of the increase to expenditures was the result of the commencement of the \$64 million State Penitentiary Building Project, increased extraordinary repair costs, increased RRI expenditures, and increased salary and benefits costs.

Analysis of Significant Changes in Operations

During the biennium ended June 30, 2011, the Department of Corrections and Rehabilitation commenced the \$64 million dollar State Penitentiary Building Project. The significant completion date of this project is December 2012. The project scope includes the construction of the following:

- Administration Segregation Unit – 108 beds
- General Housing Unit – 180 beds
- Intake / Orientation Unit – 120 beds
- Medical Unit – 23 beds

- North Dakota State Penitentiary (NDSP) Entrance / Department of Corrections and Rehabilitation Administration Building
- NDSP Warehouse
- NDSP Guard Tower
- Security Fencing
- Building Demolition
 - East Cell House
 - DOCR Administration Building
 - NDSP Warehouse
 - Warden's Residence
 - Deputy Warden's Residence

Analysis of Significant Variances - Budgeted and Actual Expenditures

Excluding the \$47.3 million carried over from the 2009-2011 biennium to the 2011-2013 biennium for on-going capital projects, the Department of Corrections and Rehabilitation ended the 2009-2011 biennium with \$6.9 million. \$2.9 million of that amount is general fund authority with the remaining amount of \$4.0 million being other fund authority.

The majority of the other fund authority is a result of RRI aggressive budgeting. RRI employs the philosophy of aggressive budgeting in order to respond to additional sales and business opportunities when they arise. The general fund amount of unexpended authority is a result of lower than anticipated inmate populations placed under the supervision and control of the department.

Financial Statements

Statement of Revenues and Expenditures

	<u>June 30, 2011</u>	<u>June 30, 2010</u>
<u>Revenues and Other Sources:</u>		
Roughrider Industries Sales	\$ 7,366,820	\$ 4,981,961
Federal Revenue	3,333,281	3,054,645
Correctional Fees	1,297,787	1,299,244
Meal Sales	437,536	483,585
Revenue from Counties	270,342	394,871
Mineral Lease Royalties	105,415	154,147
Interest Earnings	101,665	143,599
Miscellaneous Revenue	143,012	194,468
Transfers In	1,446,708	1,363,575
Total Revenues and Other Sources	\$ 14,502,565	\$ 12,070,095
<u>Expenditures and Other Uses:</u>		
Roughrider Industries Expenditures	\$ 6,790,042	\$ 6,035,707
Salaries and Benefits	44,264,050	42,533,602
New Building Construction Costs	15,107,060	4,072,738
Community Housing and Programming	9,084,242	9,421,904
Contract Housing	6,473,285	5,913,556
Medical, Hospital, Dental, Optical	4,644,274	4,714,849
Food and Clothing	2,921,545	2,659,998
Grants	2,884,599	2,351,453
Buildings and Grounds	2,203,248	1,049,847
Utilities	1,612,605	1,400,218
IT – Processing/Services/Equipment	1,584,753	1,513,052
Travel	774,446	812,816
Professional Service/Supply/Material	614,183	509,040
Equipment	408,136	210,858
Inmate Wages	403,781	383,817
Rent of Building Space	378,062	372,104
Supplies	343,364	255,201
Repairs	343,095	653,125
Professional Development	300,549	199,315
Insurance	118,026	166,808
Other Expenses	618,859	414,512
Total Expenditures and Other Uses	\$ 101,872,203	\$ 85,644,519

Statement of Appropriations

For The Biennium Ended June 30, 2011

Expenditures by Line Item:	<u>Original Appropriation</u>	<u>Adjustments</u>	<u>Final Appropriation</u>	<u>Expenditures</u>	<u>Unexpended Appropriation</u>
Capital					
Construction Carryover		\$ 941,102	\$ 941,102	\$ 721,713	\$ 219,389
Deferred					
Maintenance	\$ 1,372,519		1,372,519	1,196,991	175,528
Federal Stimulus Funds - 2009	1,039,856		1,039,856	609,199	430,657
Shelter & Assessment Program	200,000		200,000	200,000	
Adult Services	207,655,868	4,360,831	212,016,699	159,689,874	52,326,825
Youth Services	25,334,331	860,932	26,195,263	25,061,933	1,133,330
Totals	<u>\$ 235,602,574</u>	<u>\$ 6,162,865</u>	<u>\$ 241,765,439</u>	<u>\$ 187,479,710</u>	<u>\$ 54,285,729</u>
Expenditures by Source:					
General Fund	\$ 164,090,829	\$ 4,002,084	\$ 168,092,913	\$ 162,428,048	\$ 5,664,865
Other Funds	71,511,745	2,160,781	73,672,526	25,051,662	48,620,864
Totals	<u>\$ 235,602,574</u>	<u>\$ 6,162,865</u>	<u>\$ 241,765,439</u>	<u>\$ 187,479,710</u>	<u>\$ 54,285,729</u>

Appropriation Adjustments:

The \$941,102 increase in the Capital Construction Carryover line was approved by the Construction Carryover Committee.

The \$4,360,831 increase to the Adult Services line was a combination of \$2,503,933 for salary increases provided by Senate Bill 2015, section 4 of the 2009 session laws, and \$1,730,000 for the management and operation of the prison's commissary, \$122,656 to implement a workforce training project in partnership with Bismarck State College for prison inmates, and \$4,242 for the State Government Internship Stipend Program which were approved by the Emergency Commission.

The \$860,932 increase to the Youth Services line consisted of \$546,067 for salary increases provided by Senate Bill 2015, section 4 of the 2009 session laws, and \$308,125 for energy improvements and \$6,740 for the State Government Internship Stipend Program approved by the Emergency Commission.

Expenditures Without Appropriations Of Specific Amounts:

Insurance recoveries has a continuing appropriation authorized by NDCC section 54-44.1-09.1 (\$37,012 of expenditures for this biennium).

Internal Control

In our audit for the biennium ended June 30, 2011, we identified the following areas of the Department of Corrections and Rehabilitation's internal control as being the highest risk:

Internal Controls Subjected to Testing:

- Controls surrounding the processing of revenues at Roughrider Industries.
- Controls surrounding the processing of expenditures at Roughrider Industries.
- Controls surrounding the processing of expenditures for Adult Services and Youth Services.
- Controls surrounding purchases made using P-cards.
- Controls effecting the safeguarding of pharmacy and Roughrider Industries inventory.
- Controls surrounding inmate accounts.
- Controls relating to compliance with legislative intent.
- Controls surrounding the ConnectND (PeopleSoft) system.
- Controls surrounding the Macola information 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 certain matters involving internal control and its operation that we consider to be significant deficiencies.

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 deficiencies in internal control. We also noted other matters involving internal control that we have reported to management of Department of Corrections and Rehabilitation in a management letter dated March 27, 2012.

Lack of Controls Over Pharmacy Inventory (Finding 11-1)

Condition:

The Department of Corrections and Rehabilitation does not have an inventory system that enables them to accurately account for returned medication and inventory balances.

Criteria:

The Committee of Sponsoring Organizations (COSO) guidelines on control activities states “Control policies and procedures must be established and executed to help ensure the actions identified by management as necessary to address risks to achievement of the entity’s objectives are effectively carried out.”

Cause:

The current inventory system is not capable of perpetual inventory record keeping.

Effect or Potential Effect:

Potential discrepancies could go undetected.

Recommendation:

We recommend the Department of Corrections and Rehabilitation establish an inventory system that will enable the agency to accurately account for returned medication and inventory balances.

Department of Corrections and Rehabilitation Response:

The Department of Corrections and Rehabilitation (DOCR) agrees with this recommendation. The DOCR is currently working with its electronic medical record (EMR) vendor to address this finding. A new version of EMR application, which will have the capability of accounting for returned medications is scheduled to be deployed in January 2013. Mitigating controls surrounding the purchase, receipt, and disbursement of medications from pharmacy have been and will continue to be in place until the EMR application can properly account for returned medications.

Control Weaknesses at Roughrider Industries (Finding 11-2)

Condition:

Roughrider Industries does not have adequate controls in place to ensure assets are adequately safeguarded and financial transactions are properly recorded.

The following control weaknesses were identified at Roughrider Industries:

- Access to cash is not restricted. The individual responsible for opening the mail does not restrictively endorse the checks or create a remittance list. Cash is then passed to the individual responsible for preparing the deposit. Individuals with access to cash also have access in the Macola system to credit/write-off receivables. In addition, there is no report from the Macola system to ensure all adjustments to receivables are properly approved.
- The individual responsible for reviewing batch totals for the credit card machine can accept credit cards and make adjustments to accounts receivable in Macola.
- Inventory adjustment reports are not consistently run, maintained on file, and appropriately approved by an individual that does not have custody of stock.
- The access role that enables individuals to make inventory and pricing adjustments in Macola is not limited to appropriate individuals. Macola uses generalized IDs that multiple individuals have access to, including inmates.
- The individual responsible for preparing the bank reconciliation has access in Macola to create accounts payable, and has access to checks.
- There are no controls in place to ensure all payments are made to an appropriate vendor.
- Application/Eligibility determinations were not properly completed.
- Raises and bonuses/commissions were not properly supported.
- Fixed Asset report is prepared by the individual with access to make adjustments and not approved by an appropriate individual.
- Lack of procurement records for certain purchases.
- Purchase card reconciliations were not properly approved.
- Meal purchases were not approved, supported, or subject to income tax if no overnight stay was required.

Criteria:

The Committee of Sponsoring Organizations (COSO) defines segregation of duties to have duties divided or separated to reduce the risk of error or inappropriate action.

OMB Procurement Guidelines details procedures requirements for purchasing items for state use.

OMB Policy 505 requires reimbursement for meals which did not involve overnight travel to be included in the individual's wages and subject to income tax.

North Dakota Century Code chapter 54-46 details the records retention schedule and audit standards require the use of original documents as support for testing.

Cause:

Client oversight.

Effect or Potential Effect:

Potential discrepancies could go undetected.

Recommendation:

We recommend the Department of Corrections and Rehabilitation:

- Properly segregate duties surrounding cash receipts, accounts receivable, inventory, and fixed assets at Roughrider Industries.
- Ensure sales are made to eligible businesses.
- Ensure raises and bonuses/commissions are properly supported.

Department of Corrections and Rehabilitation Response:

The Department of Corrections and Rehabilitation (DOCR) agrees with this recommendation. The DOCR conducted an internal investigation of Roughrider Industries in the spring of 2011 which uncovered numerous management and operational deficiencies within Roughrider Industries (resultant report provided to State Auditor's Office at commencement of the audit). As a direct result of that investigation, both the director and the sales manager of Roughrider Industries were immediately terminated from employment. New management is in place at Roughrider Industries and has addressed the weakness noted above. Where possible, duties involving ordering, receiving, recording, deposit and disbursement are now properly segregated. If proper segregation of duties is not possible due to staffing limitations, mitigating controls have been implemented.

Compliance With Legislative Intent

In our audit for the biennium ended June 30, 2011, we identified and tested Department of Corrections and Rehabilitation's compliance with legislative intent for the following areas we determined to be significant and of higher risk of noncompliance:

- Compliance with the requirement to contract with a private nonprofit organization with appropriated funds of \$200,000 to establish a short-term shelter, assessments, and intervention services for at-risk youth program in the south central judicial district. (2009 North Dakota Session Laws chapter 476, sections 1 and 2).
- Compliance with the \$5,000 limit on awards from the Crime Victim Compensation fund for funeral expenses of crime victims. (North Dakota Century Code 54-23.4-01).
- Compliance with the requirement to have either the director of the Department of Corrections and Rehabilitation or the director's designee on the Criminal Justice Information Sharing Board. (North Dakota Century Code 54-59-21).
- Compliance with equity pool guidelines for increases to pay grades one through fourteen (2009 North Dakota Session Laws chapter 43, section 4).
- Compliance with the following special appropriations:
 - Contingent funding of \$93,592 from the general fund for roof repairs for the Missouri River Correctional Center if not relocated to the State Penitentiary (2009 North Dakota Session Laws chapter 43, section 5).
 - Contingent funding of \$419,743 from the general fund for temporary housing of sexual offenders, boiler repairs, and other heating and cooling equipment replacement (2009 North Dakota Session Laws chapter 43, section 6).
 - Distribution in the sum of \$1,628,813 to the Heart of America Correction and Treatment Center for inmate-related treatment services (2009 North Dakota Session Laws chapter 43, section 7).
- Compliance with the requirement to establish controls to ensure wireless communication devices are prohibited in correctional facilities (North Dakota Century Code 12-47-21).
- Compliance with the requirement to employ personnel and establish policies and procedures to supervise sexually dangerous individuals released to community placement on an outpatient basis (North Dakota Century Code 25-03.3-24).
- Proper use of the following legally restricted funds:
 - Community Service Supervision fund.
 - Probationer Violation Transportation fund.
 - State Penitentiary Land fund.
 - Crime Victims Restitution and Gift fund.
- Application of proper statutory rates relating to revenue.
- Proper use of the State Treasurer (State Constitution, article X, section 12).
- Compliance with appropriations and related transfers (2009 North Dakota Session Laws chapter 43).
- Compliance with OMB's Purchasing Procedures Manual.

- Travel-related expenditures are made in accordance with OMB policy and state statute.
- 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 has occurred or is likely to have occurred.

The results of our tests disclosed two instances of noncompliance that are required to be reported under *Government Auditing Standards*. These findings are described below. Other than those findings, we concluded there was compliance with the legislative intent identified above. We also noted certain inconsequential instances of noncompliance that we have reported to management of the Department of Corrections and Rehabilitation in a management letter dated March 27, 2012.

Sales to Inappropriate Vendors (Finding 11-3)

Condition:

Roughrider Industries was selling products to unauthorized vendors and not charging sales tax on sales of products that were not for resale by the vendors.

Criteria:

North Dakota Century Code section 12-48-03.1 states that all products made in prison industries may be purchased directly by governmental agencies, including federal, state, and tribal agencies and political subdivisions for use in official business, and by nonprofit organizations, excluding trade associations, fraternal organizations, co-ops, and health insurance companies. Prison industries-made products may also be sold through wholesale or retail outlets that possess a valid sales tax permit.

North Dakota Century Code section 57-39.2-02.1 imposes a 5% tax on the gross receipts of retailers for retail sales.

Cause:

Lack of oversight by management.

Effect:

Noncompliance with North Dakota Century Code.

Recommendation:

We recommend the Department of Corrections and Rehabilitation strengthen controls over Roughrider Industries sales to ensure all sales are to authorized vendors. Further, the Department of Corrections and Rehabilitation should consult with the Office of the State Tax Commissioner to determine if any additional sales tax is due.

Department of Corrections and Rehabilitation Response:

The Department of Corrections and Rehabilitation (DOCR) agrees with this recommendation. The DOCR conducted an internal investigation of Roughrider Industries in the spring of 2011 which uncovered numerous management and operational deficiencies within Roughrider Industries (resultant report provided to State Auditor's Office at commencement of the audit). As a direct result of that investigation, both the director and the sales manager of Roughrider Industries were immediately terminated from employment. New management is in place at Roughrider Industries and is aware of and in compliance with state laws governing the sale of products made by prison industries. In addition, the Office of the State Tax Commissioner will be consulted regarding the sales tax issue.

Improper Use of Public Funds (Finding 11-4)**Condition:**

Many instances of Roughrider Industries expenditures were identified to be in violation of state laws and OMB policy. The Department of Corrections and Rehabilitation was aware of these issues prior to the start of this audit and had conducted their own internal investigation.

Improper expenditures include:

- Meals were purchased for inmates at restaurants while assisting with delivery of Roughrider Industries products, despite the fact that those inmates may have been provided sack lunches before leaving the Missouri River Correctional facility. Further, many of these meals exceeded per diem provided to state employees and were made using state issued purchase cards.
- Purchase of coffee for use by inmate workers and Roughrider Industries staff.
- Lack of receipts for cash taken from the petty cash account.
- Lunch provided to staff and private individuals without itemized receipts or in excess of per diem rates with no support as to 'promotional' nature of meeting.
- Purchase of food items for occasional 'incentive' parties for inmate workers and Roughrider Industries staff, which included purchasing steak for one party.
- Advances on payroll bonuses not yet earned.
- An employee claimed and was reimbursed for meals which were provided by a conference.

Criteria:

Office of Management and Budget Policy 300 states that purchase cards can be used for all travel expenses except meals.

Department of Corrections and Rehabilitation Policy 14A-6 provides Missouri River Correctional Center inmates with sack lunch when delivering in the Bismarck/Mandan area.

Office of Management and Budget Policy 515 states that beverages can be provided only in instances where the public, interested parties or consultants will be present for informative or training purposes.

Roughrider Industries Policy 2A-3 requires receipts for all purchases from petty cash fund.

There is no authorization that would allow for payroll advances or use of Roughrider Industries funds to purchase food for 'incentive' meals.

North Dakota Century Code section 44-08-04 states that if meals are included in conference registration fees, they cannot be claimed for reimbursement.

Cause:

Lack of oversight by management.

Effect:

The Department of Corrections and Rehabilitation is not in compliance with North Dakota Century Code, Office of Management and Budget Policies, and Department of Correction and Rehabilitation policies and the use of state funds for unauthorized purposes.

Recommendation:

We recommend the Department of Corrections and Rehabilitation strengthen controls surrounding expenditures at Roughrider Industries to ensure compliance with North Dakota Century Code, Office of Management and Budget policies, and agency policies.

Department of Corrections and Rehabilitation Response:

The Department of Corrections and Rehabilitation (DOCR) agrees with this recommendation. The DOCR conducted an internal investigation of Roughrider Industries in the spring of 2011 which uncovered numerous management and operational deficiencies within Roughrider Industries (resultant report provided to State Auditor's Office at commencement of the audit). As a direct result of that investigation, both the director and the sales manager of Roughrider Industries were immediately terminated from employment. New management is in place at Roughrider Industries and is aware of and in compliance with state laws governing the use of state funds, and OMB and DOCR fiscal and administrative policies.

Operations

This audit did not identify areas of Department of Corrections and Rehabilitation'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 management of the Department of Corrections and Rehabilitation in a management letter dated March 27, 2012.

Management Letter (Informal Recommendations)

March 27, 2012

Ms. Leann Bertsch, Director
Department of Corrections and Rehabilitation
3100 Railroad Avenue
Bismarck, ND 58501

Dear Ms. Bertsch:

We have performed an audit of the Department of Corrections and Rehabilitation for the biennium ended June 30, 2011, and have issued a report thereon. As part of our audit, we gained an understanding of the Department of Corrections and Rehabilitation'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 11-1: We recommend the Department of Corrections and Rehabilitation properly segregate duties surrounding the collection of supervision fees.

EXPENDITURES

Informal Recommendation 11-2: We recommend the Department of Corrections and Rehabilitation establish policies and procedures to ensure payments to crime victims are made consistently to eligible individuals for expenses incurred in accordance with NDCC 54-23.4-06.

ASSETS/INVENTORY

Informal Recommendation 11-3: We recommend the Department of Corrections and Rehabilitation strengthen controls surrounding fixed assets to ensure records are complete and individuals without access to computerized records are taking inventory.

LEGISLATIVE INTENT

Informal Recommendation 11-4: We recommend the Department of Corrections and Rehabilitation implement controls to ensure travel and meal reimbursements are properly authorized and supported.

Informal Recommendation 11-5: We recommend the Department of Corrections and Rehabilitation properly procures goods and services in accordance with State Procurement policies and insure that all purchase card holders have adequate procurement training.

OPERATIONAL

Informal Recommendation 11-6: We recommend the Department of Corrections and Rehabilitation use their purchase card as a form of payment to all vendors accepting purchase cards.

Management of Department of Corrections and Rehabilitation 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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Office of the State Auditor
600 East Boulevard Avenue – Department 117
Bismarck, ND 58505-0060

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