

# INDUSTRIAL COMMISSION

## BISMARCK, NORTH DAKOTA

Department of Mineral Resources  
Lignite Research Program  
Oil and Gas Research Program  
Renewable Energy Program  
Pipeline Authority  
Transmission Authority  
Outdoor Heritage Fund

# Audit Report

For the Biennium Ended  
June 30, 2015



Office of the State Auditor  
Division of State Audit

**LEGISLATIVE AUDIT AND FISCAL REVIEW  
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## *Transmittal Letter*

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April 12, 2016

The Honorable Jack Dalrymple, Governor  
Members of the North Dakota Legislative Assembly  
Ms. Karlene Fine, Executive Director, Industrial Commission

We are pleased to submit this audit of the Industrial Commission for the biennium ended June 30, 2015. 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 Michael W. Schmitcke, CPA. Kevin Scherbenske, CPA, and Amanda Westlake 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 Karlene Fine, Lynn Helms, and their 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 Industrial Commission was created by the Legislature in 1919 to conduct and manage, on behalf of the state, certain utilities, industries, enterprises, and business projects established by state law. The members of the Industrial Commission are the Governor, Attorney General, and the Agriculture Commissioner of the state.

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 Industrial Commission 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 unmodified 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 finding addressing "untimely approval of meeting minutes" (page 14), the Industrial Commission 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?*

Yes.

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

There were not any indications of a lack of efficiency in financial operations and management of the Industrial Commission, although in our operational work addressing "lack of support for in-kind matching" (page 16), we did note an area where greater efficiency could be achieved.

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

The only finding from the prior audit was implemented.

### *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 18 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 Industrial Commission'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), and the Risk Based Data Management System (RBDMS) are high-risk information technology systems critical to the Industrial Commission.

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

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## ***Audit Objectives***

The objectives of this audit of the Industrial Commission for the biennium ended June 30, 2015 were to provide reliable, audited financial statements and to answer the following questions:

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

## ***Audit Scope***

This audit of the Industrial Commission is for the biennium ended June 30, 2015. 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 Industrial Commission has operations in the following locations. Each location was included in the audit scope:

- Administrative office in the State Capitol.
- Department of Mineral Resources office, Bismarck.
- Core and Sample Library, Grand Forks.
- Regional offices in Dickinson, Minot, and Williston.

## ***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 the Industrial Commission's processes and procedures.
- Performed a detailed review of the Outdoor Heritage Fund grant program.

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***

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The accompanying financial statements have been prepared to present the Industrial Commission'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 Industrial Commission'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, 2015, operations of the Industrial Commission were primarily supported by appropriations from the state's general fund and special funds.

### ***Financial Summary***

Total Revenues and Other Sources for the Industrial Commission was \$20,550,667 in fiscal year 2015, compared to \$34,631,635 in fiscal year 2014. Revenues unique to the Commission include revenues from an investment made through the Lignite Research Program in the Dakota Gasification Company (DGC). The provisions of the Investment Agreement state the annual repayment to the Lignite Research Fund is linked to a formula based percentage of DGC's net income. DGC had a profitable year in 2015.

Fines were higher in 2015 as a result of enforcement actions in response to oil, water, and gas releases caused by well bore and reserve pit failures. Significant rule changes have been implemented to eliminate subsequent similar failures. The remaining revenues came from federal funds, investment earnings on the research funds, charges for services, permits, and fees.

Transfers in were lower in 2015 than in 2014. State law authorizes that 2% of the revenues from the oil and gas gross production tax and oil extraction tax, up to \$10 million per biennium, must be deposited monthly in the oil and gas research fund. With the state receiving increased revenues from these two taxes the entire \$10 million in revenues was received during fiscal year 2014. State law authorizes that 5% of the revenues from the oil and gas gross production tax and oil extraction tax, up to \$3 million per biennium, must be deposited monthly in the renewable energy development fund. With the state receiving increased revenues from these two taxes the entire \$3 million in revenues was received during fiscal year 2014.

Total expenditures and other uses for the Industrial Commission were \$19,926,011 for the year ended June 30, 2014, as compared to \$15,045,655 for the prior year (2013). In 2015 there was an increase to \$25,197,077 based partially on salaries and benefits. By the end of the fiscal year 2015 the positions authorized by the Legislature in 2013 had all been filled.

Grant expenditures increased in fiscal year 2015 as a result of when work was completed under the research programs. Also, there were more grant expenditures in fiscal year 2015 for the Outdoor Heritage program as it was just getting organized in fiscal year 2014.

Professional Services increased due to the start of federal regulatory over-reach litigation; increases in reclamation; and Geological Survey one-time special funded projects.

Transfers Out decreased in 2015 due to one-time biennium transfers from funds to Industrial Commission Administration occurring during 2014.

The Commission's oversight also includes the Abandoned Oil and Gas Reclamation Fund. On June 30, 2015 the balance in this fund was \$11,538,379. Revenues to the fund must include:

- Fees collected by the Oil and Gas Division of the Industrial Commission for permits or other services.
- Moneys received from the forfeiture of drilling and reclamation bonds.
- Moneys received from any federal agency for the purpose of this section.
- Moneys donated to the Commission for the purposes of this section.
- Moneys received from the state's Oil and Gas Impact Fund.
- Moneys recovered under the provisions of Section 38-08-04.8.
- Moneys recovered from the sale of equipment and oil confiscated under section 38-08-04.9.
- Moneys transferred from the Cash Bond Fund under Section 38-08-04.11.
- Such other moneys as may be deposited in the fund for use in carrying out the purposes of plugging or re-plugging of wells or the restoration of well sites.
- Civil penalties assessed under section 38-08-16.

Monies in this fund are appropriated and must be used and disbursed solely for the purpose of defraying the costs in carrying out the plugging or re-plugging of wells, the reclamation of well sites, and all other related activities. The 2013 Legislature increased the funding level for this fund and expanded the types of projects for which these funds can be utilized.

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

Oil and gas development remained at historic levels during fiscal years 2014 and 2015. In December 2013, there were 190 drilling rigs and 10,053 producing wells operating in the state - production for calendar year 2013 was 313,812,250 barrels of oil. In December 2014, there were 12,142 producing wells operating in the state—production for calendar year 2014 was 396,880,762 barrels of oil. In calendar year 2014, the drilling rig count peaked at 195 in September and averaged 190 drilling rigs with the count being 181 in December of 2014. During the remainder of the 2013-2015 biennium, the rig count has dropped from 181 to 78 and oil production is relatively flat, although the producing well count has continued to increase. This historic level of activity has created a significant workload for the Industrial Commission.

During the 2013 Legislative Session two new programs/responsibilities were given to the Industrial Commission. House Bill No. 1278 established the Outdoor Heritage Fund and authorized up to \$30,000,000 per biennium with funding coming from a percentage of the oil and gas production taxes. Actual revenues were \$9,962,504 for the 2014 fiscal year and \$8,688,237 for the 2015 fiscal year. No additional full-time staffing was hired to administer this program and this workload was handled by the current staff (Administrative Office and Industrial Commission accounting staff located at the Department of Mineral Resources offices) and some part-time temporary staffing. The Legislature also directed that the Commission have oversight of the Western Area Water Supply Authority industrial water sales (Senate Bill No. 2233). A full-time staff person was authorized in the legislation but the Commission's appropriation was not

increased to allow expenditures for the position. This workload was also assumed by the current Industrial Commission staff.

### ***Analysis of Significant Variances - Budgeted and Actual Expenditures***

The Commission continued to see unexpended appropriation authority in its grants line item. This is a result of the timing of payments for Lignite Research Program Projects. Payments are made on projects based on work accomplished. Because of uncertainty at the federal level on energy issues, one Lignite Vision 21 project has been delayed and another project has returned their commitment. The Commission had committed Lignite Research Fund dollars in the approximate amount of \$14 million for these two projects. The project being undertaken by Great Northern Power Development near South Heart has been delayed and in January 2015 the American Lignite Energy Project in McLean County was withdrawn and the commitment of \$8,615,000 was released. If issues at the federal level are resolved, we are hopeful that the project at South Heart will move forward.

There were unexpended Salaries and Benefits due to a \$445,185 required turn back resulting from a legislative council calculation error in House Bill 2014; approximately \$363,000 from contingent FTEs not being triggered until July 2014 and difficulties in filling the positions; and \$460,953 from the Public Finance Authority appropriated funds which are not run through PeopleSoft. Of the unexpended Operating Expenses \$874,025 was a carryover from the one-time funding for possible federal agency litigation, and \$225,600 from the Public Finance Authority appropriated funds, which are not run through PeopleSoft.

# Financial Statements

## Statement of Revenues and Expenditures

	<u>June 30, 2015</u>	<u>June 30, 2014</u>
<b><u>Revenues and Other Sources:</u></b>		
Charges for Sales and Services	\$ 539,253	\$ 733,493
Permits and Fees	674,210	643,173
Donations	500	310,000
Fines	302,740	207,904
Refund of Prior Biennium Expenditure	275,000	
Federal Revenue	7,350	105,350
Interest and Investment Earnings	21,268	17,253
Dakota Gasification Company Loan Revenue	74,760	
Miscellaneous Revenue	5,971	27,897
Transfers In	18,649,615	32,586,565
<b>Total Revenues and Other Sources</b>	<b><u>\$ 20,550,667</u></b>	<b><u>\$ 34,631,635</u></b>
<b><u>Expenditures and Other Uses:</u></b>		
Salaries and Benefits	\$ 9,083,700	\$ 8,067,256
Grants	10,559,997	8,116,887
Professional Services	3,042,443	961,909
Travel	847,019	739,763
Rentals/Leases – Buildings	361,172	724,678
Data Processing/Communications	199,519	177,839
Supplies	190,357	147,037
Equipment	74,162	145,786
Equipment under \$5000	385,142	124,408
Operating Fees and Services	114,608	75,540
Professional Development	117,671	53,389
Miscellaneous Operating Expenses	162,521	143,519
Transfers Out	58,766	448,000
<b>Total Expenditures and Other Uses</b>	<b><u>\$ 25,197,077</u></b>	<b><u>\$ 19,926,011</u></b>

## Statement of Appropriations

For The Biennium Ended June 30, 2015

<b>Expenditures by Line Item:</b>	<u>Original Appropriation</u>	<u>Adjustments</u>	<u>Final Appropriation</u>	<u>Expenditures</u>	<u>Unexpended Appropriation</u>
Salaries and Benefits	\$ 17,873,876	\$ 293,849	\$ 18,167,725	\$ 16,660,723	\$ 1,507,002
Accrued Leave Payments	347,696		347,696	23,688	324,008
Operating Expenses	5,930,576	106,151	6,036,727	4,740,390	1,296,337
Capital Assets	5,800		5,800	2,673	3,127
Grants	19,500,000		19,500,000	5,155,860	14,344,140
<b>Totals</b>	<u>\$ 43,657,948</u>	<u>\$ 400,000</u>	<u>\$ 44,057,948</u>	<u>\$ 26,583,334</u>	<u>\$ 17,474,614</u>
<b>Expenditures by Source:</b>					
General Fund	\$ 22,494,125	\$ 400,000	\$ 22,894,125	\$ 20,775,219	\$ 2,118,906
Other Funds	21,163,823		21,163,823	5,808,115	15,355,708
<b>Totals</b>	<u>\$ 43,657,948</u>	<u>\$ 400,000</u>	<u>\$ 44,057,948</u>	<u>\$ 26,583,334</u>	<u>\$ 17,474,614</u>

### Appropriation Adjustments:

The increase to the Salaries and Benefits line item and Operating Expenses line item was a supplemental appropriation made by the 2013 Legislative Assembly under section 6 of House Bill 1015. These adjustments were approved by the Emergency Commission. The funds are for rental assistance and temporary salary increases in areas affected by energy development.

### Expenditures Without Appropriations Of Specific Amounts:

Fossil Excavation and Restoration Fund has a continuing appropriation authorized by NDCC section 54-17.4-09.1 (\$19,907 of expenditures for this biennium).

Renewable Energy Development Fund has a continuing appropriation authorized by NDCC section 54-63-04 (\$2,266,304 of expenditures for this biennium).

Oil and Gas Research Fund has a continuing appropriation authorized by NDCC section 57-51.1-07.3 (\$9,465,780 of expenditures for this biennium).

Carbon Dioxide Storage Facility Administrative Fund has a continuing appropriation authorized by NDCC section 38-22-14 (\$57,293 of expenditures for this biennium).

Pipeline Authority Administrative Fund has a continuing appropriation authorized by NDCC section 54-17.7-11 (\$214,810 of expenditures for this biennium).

North Dakota Outdoor Heritage Fund has a continuing appropriation authorized by NDCC section 54-17.8-02 (\$2,476,720 of expenditures for this biennium).

Cash Bond Fund has a continuing appropriation authorized by NDCC section 38-08-04.11 (\$73,329 of expenditures for this biennium).

Cartographic Products Fund has a continuing appropriation authorized by NDCC section 54-17.4-10 (\$93 of expenditures this biennium).

Global Positioning System Community-base Station Fund has a continuing appropriation authorized by NDCC section 54-17.4-12 (\$450 of expenditures this biennium).

Oil and Gas Reservoir Data Fund has a continuing appropriation authorized by NDCC section 38-08-04.6 (\$758,993 of expenditures for this biennium).

Geo Data Preservation Fund has a continuing appropriation authorized by NDCC section (\$77,628 of expenditures for this biennium).

Geo Mineral Coal Exploration Fund has a continuing appropriation authorized by NDCC section 38-21-01 (\$134 of expenditures for this biennium).

Abandoned Oil and Gas Reclamation Fund has a continuing appropriation authorized by NDCC section 38-08-04.5 (\$2,150,437 of expenditures for this biennium).

## ***Internal Control***

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In our audit for the biennium ended June 30, 2015, we identified the following areas of the Industrial Commission'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.

The criteria used to evaluate internal control is published in the publication *Standards for Internal Control in the Federal Government* issued by the Comptroller General of the United States (Green Book, GAO-14-704G). Agency management must establish and maintain effective internal control in accordance with Office of Management and Budget (OMB) Policy 216 and, for programs receiving federal funds, the Code of Federal Regulation as set forth by the federal government (2 CFR 200.303).

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 internal control was adequate.

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 did not identify any significant deficiencies in internal control. However, we noted a matter involving internal control that we have reported to management of the Industrial Commission in a management letter dated April 12, 2016.



## *Compliance With Legislative Intent*

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In our audit for the biennium ended June 30, 2015, we identified and tested the Industrial Commission's compliance with legislative intent for the following areas we determined to be significant and of higher risk of noncompliance:

- Compliance with appropriations of \$647,547 for administrative services rendered by the Commission (Senate Bill 2014, section 6 of the 2013 Legislative Session).
- Compliance with appropriations of \$4,500,000 to contract for an independent, nonmatching lignite marketing feasibility study (Senate Bill 2014, section 17 of the 2013 Legislative Session).
- Compliance with appropriations of \$150,000 to perform nonmatching studies related to the oil and gas industry (Senate Bill 2014, section 18 of the 2013 Legislative Session).
- Compliance with appropriations of \$586,230 to hire three full-time equivalent positions (Senate Bill 2014, section 19 of the 2013 Legislative Session).
- Compliance with appropriations of \$5,000,000 to provide distributions to eligible counties experiencing new oil and gas development activities (House Bill 1358, section 9 of the 2013 Legislative Session).
- Industrial Commission to place wells in abandoned-well status which have not produced oil or natural gas in paying quantities for one year (NDCC 38-08-04).
- Proceeds from the sale of equipment and salable oil to cover plugging costs of a well were properly deposited into the Abandoned Oil & Gas Well Plugging and Site Reclamation Fund (NDCC 38-08-04.8).
- Proper use of the following legally restricted funds:
  - Fossil Excavation & Restoration Fund (NDCC 54-17.4-09.1).
  - Renewable Energy Development Fund (NDCC 54-63-04).
  - Oil & Gas Research Fund (NDCC 57-51.1-07.3).
  - Pipeline Authority Administrative Fund (NDCC 54-17.7-11).
  - North Dakota Outdoor Heritage Fund (NDCC 54-17.8-02).
  - Lignite Research Fund (NDCC 57-61-01.6).
  - Geo Mineral Coal Exploration Fund (NDCC 38-21-02).
  - Abandoned Oil & Gas Well Plugging and Site Reclamation Fund (NDCC 38-08-04.5).
- Proper use of the State Treasurer (State Constitution, article X, section 12).
- Compliance with appropriations and related transfers (2013 North Dakota Session Laws chapter 45).
- Compliance with OMB's Purchasing Procedures Manual.
- Travel-related expenditures are made in accordance with OMB policy and state statute.
- Proper authorization of petty cash funds.
- Proper authority for investments.
- Adequate blanket bond coverage of employees (NDCC section 26.1-21-08).
- Compliance with fixed asset requirements including record-keeping and inventory.



- Proper fund authorization.
- Proper use of the Bank of North Dakota as a processing depository for credit card activity (NDCC section 54-06-08.2).
- Compliance with payroll-related laws including statutory salaries for applicable 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 one instance of noncompliance that is required to be reported under *Government Auditing Standards*. This finding is described below. Other than that finding, we concluded there was compliance with the legislative intent identified above. We also noted an inconsequential instance of noncompliance that we have reported to management of the Industrial Commission in a management letter dated April 12, 2016.

### ***Untimely Approval of Meeting Minutes (Finding 15-1)***

#### **Condition:**

The meeting minutes of the Industrial Commission were not reviewed and approved by Industrial Commission members in a timely manner. A majority of the meeting minutes taken for meetings that took place during the biennium under audit were not reviewed and approved by the Industrial Commission until the February 16, 2016 meeting.

#### **Criteria:**

Attorney General Opinion 98-O-04 states “draft minutes must usually be prepared and available before the next regular meeting of the public entity.”

Attorney General Opinion 98-O-25 states “generally, draft minutes should be prepared shortly after a meeting and approved at the governing body’s next meeting.”

Further, Attorney General Opinion 2014-O-06 concluded “The North Dakota Industrial Commission violated open records law when it failed to provide requested records within a reasonable time.”

#### **Cause:**

Lack of proper procedures established by the Industrial Commission.

#### **Effect or Potential Effect:**

Without proper review and approval by Industrial Commission members, the meeting minutes may contain errors and inaccuracies in the official record of the Industrial Commission’s actions.

**Recommendation:**

We recommend the Industrial Commission ensure meeting minutes are prepared timely and approve the minutes at the Industrial Commission's next meeting.

***Industrial Commission Response:***

*The Industrial Commission agrees with the finding and recommendation. The Industrial Commission has begun the process of hiring additional staff and has directed the Industrial Commission Executive Director and Secretary provide draft minutes to the Commission for their consideration at their next regularly scheduled monthly meetings. Since the beginning of 2016 this has been done and the non-confidential Industrial Commission meeting minutes are being posted on the Industrial Commission's website.*

## *Operations*

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Our audit of the Industrial Commission identified an area of potential improvement to the agency's operations, as expressed by our operational objective:

- Is the Outdoor Heritage Fund program implemented by the Industrial Commission operating efficiently and effectively and in compliance with significant high-risk laws?

### ***Lack of Support for In-Kind Matching (Finding 15-2)***

#### **Condition:**

The Industrial Commission is authorized to use the Outdoor Heritage Fund to provide grants to state agencies, tribal governments, political subdivisions, and nonprofit organizations for the following reasons:

- Provide access to private and public lands for sportsmen;
- Improve, maintain, and restore water quality, soil conditions, plant diversity, animal systems, and practices of stewardship to enhance farming and ranching;
- Restore wildlife and fish habitat; and
- Conserve natural areas and create areas of recreation.

Many of the grant applications approved by the Industrial Commission during the period under audit included provisions that a portion of the project would be completed by the applicant through some form of in-kind match.

A review of 10 grant awards determined that 9 of the grant awards included in-kind match and the Industrial Commission did not have supporting documentation to show how the in-kind matching contributions were calculated or met.

#### **Criteria:**

The criteria used to evaluate internal control is published in the publications *Standards for Internal Control in the Federal Government* issued by the Comptroller General of the United States (Green Book, GAO-14-704G). Agency management must establish and maintain effective internal control according to guidance of the Green Book pursuant to Office of Management and Budget Policy 216 and, for programs receiving federal funds, the Code of Federal Regulation as set forth by the federal government (2 CFR 200. 303).

The Outdoor Heritage Fund scoring sheet used matching as one of their scoring criteria as well as stated that matching was recommended/encouraged.

#### **Cause:**

The client was unaware of the requirement to monitor and verify the in-kind match.

#### **Effect or Potential Effect:**

The grant recipients may not be providing the in-kind matching amounts stipulated in the grant agreements.

**Operational Improvement:**

We recommend the Industrial Commission implement procedures to ensure any in-kind matching claimed by a grantee is properly supported and reviewed.

***Industrial Commission Response:***

*During the 2013-2015 biennium the Industrial Commission did not require that the applicant provide a match. As noted, a matching component by the applicant was encouraged and was a criteria used in the ranking process. However, because a match was not required the Industrial Commission staff did not realize it was necessary for the applicant to provide verification of the expenditure of the matching dollars. Subsequent to the audit period the Legislature stated there must be match funding on each project and procedures have been implemented requiring documentation on any in-kind matching funds.*

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

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April 12, 2016

Ms. Karlene Fine  
Executive Director  
Industrial Commission  
600 E. Boulevard Avenue  
Bismarck, ND 58505

Dear Ms. Fine:

We have performed an audit of the Industrial Commission for the biennium ended June 30, 2015, and have issued a report thereon. As part of our audit, we gained an understanding of the Industrial Commission'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.

## **PERVASIVE CONTROLS**

Informal Recommendation 15-1: We recommend the Industrial Commission perform a fraud risk assessment at least every biennium in accordance with OMB Policy 216.

## **LEGISLATIVE INTENT**

Informal Recommendation 15-2: We recommend the Industrial Commission obtain a sufficient level of blanket bond coverage.

Management of the Industrial Commission agreed with these recommendations.

I encourage you to call me 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,

A handwritten signature in cursive script that reads "Michael W. Schmitcke".

Michael W. Schmitcke, CPA  
Auditor in-charge

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Division of State Audit

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

(701) 328-2241