

Department of Corrections  
BISMARCK, NORTH DAKOTA

# Audit Report

For the Biennium Ended  
June 30, 2015

ROBERT R. PETERSON  
STATE AUDITOR



Office of the State Auditor  
Division of State Audit

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

## *Transmittal Letter*

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January 4, 2016

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, 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 Delan Hellman. 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 cursive script that reads "Bob Peterson".

Robert R. Peterson  
State Auditor

# *Executive Summary*

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## *Introduction*

The North Dakota Department of Corrections and Rehabilitation's mission is to enhance public safety, to reduce the risk of future criminal behavior by holding adult and juvenile offenders accountable, and to provide opportunities for change. 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 unmodified opinion was issued.

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

Yes.

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

Other than our finding addressing the "Lack of Controls Over Pharmacy Inventory" (page 12), 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?*

Except "Lack of Controls Over Pharmacy Inventory" as shown on page 12, the Department of Corrections and Rehabilitation has implemented all recommendations included in the prior audit report.

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

Yes, a management letter was issued and is included on page 17 of this report, along with management's response.

## **LAFRC Audit Communications**

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

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

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

The Department of Corrections 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), and Macola are high-risk information technology systems critical to the Department of Corrections and Rehabilitation.

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

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## ***Audit Objectives***

The objectives of this audit of the Department of Corrections and Rehabilitation 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 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, 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 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 the Department of Corrections and Rehabilitation's processes and procedures.
- Performed a detailed review of Inspections of Correctional Facilities completed by the Department including:
  - Established policies and procedures;
  - Qualifications of staff;
  - Application review;
  - Inspections;
  - Complaint handling;
  - Enforcement processes; and
  - Management analysis processes.
- Performed a detailed review of the Victims of Crime Act (VOCA) grant funds including:
  - Application review;
  - Pre-award process;
  - Monitoring; and
  - Reporting.

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 Department of Corrections 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 Corrections 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, 2015, 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, prison industry revenues, and correctional fees credited to the agency's operating fund.

### ***Financial Summary***

Outside of the biennial general fund appropriation provided to the Department of Corrections and Rehabilitation, departmental 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 15% in fiscal year 2015 compared to fiscal year 2014. The majority of the increase in the revenue from 2014 to 2015 is attributable to RRI sales. Over this period of time RRI sales increased by \$1.2 million. Supervision fee revenue continues to increase due to the increasing number of individuals under supervision in the community, however due to changing economic conditions the actual collection rates of supervision fee revenue is decreasing.

Total expenditures for the Department of Corrections and Rehabilitation increased 4.6% from fiscal year 2014 to fiscal year 2015. The increase in cost is attributable to increased personnel costs, increased number of individuals incarcerated, and repayment of the State Penitentiary Building Project loan. Final payment related to the State Penitentiary Building Project was made in the fiscal year 2014, this reflected in the building expansion / extraordinary repairs account category.

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

Increased offender counts in both the community setting and in prison facilities continue to impact department operations. During the audit period the number of offenders under DOCR community supervision increased by approximately 1,200 individuals, while the DOCR inmate population increased by 205 people. To help address this increased pressure on operations, a total of 20.0 full - time equivalent (FTE) positions were added to the Department of Corrections and Rehabilitation (DOCR) authorized FTE count. Of the approved positions, 6.0 were designated to parole and probation and 14.0 were designated to the prison division.

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

Excluding the \$349,950 carried over from the 2013-15 biennium to the 2015-2017 biennium for the Missouri River Correctional Center flood control capital project, the Department of Corrections and Rehabilitation ended the 2013-2015 biennium with \$13.6 million in unexpended authority. \$3.9 million of that authority is general fund with the remaining amount being other fund authority.

The majority of the remaining amount of budgeted authority is a result of RRI aggressive budgeting and housing a larger percentage of the inmate population in DOCR facilities vs. contract facilities. RRI employs the philosophy of aggressive budgeting in order to respond to additional sales and business opportunities when they arise.

# 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>		
Roughrider Industries Sales	\$ 8,633,766	\$ 7,446,619
Correctional Fees	3,298,686	2,769,125
Federal Revenue	2,706,253	2,512,491
Meal Sales	739,830	374,750
Mineral Lease Royalties	343,489	319,404
Revenue from Counties	201,192	254,057
Reimbursement from Another State	136,194	200,680
Miscellaneous Revenue	208,111	202,158
Transfers In	1,367,879	1,320,107
<b>Total Revenues and Other Sources</b>	<b><u>\$ 17,635,400</u></b>	<b><u>\$ 15,399,391</u></b>
<b><u>Expenditures and Other Uses:</u></b>		
Roughrider Industries Expenditures	\$ 7,154,589	\$ 6,260,111
Salaries and Benefits	58,370,977	55,267,421
Community Housing and Programming	8,116,991	8,583,307
Medical, Hospital, Dental, Optical	5,933,227	5,022,538
Contract Housing	5,427,948	5,269,127
Food and Clothing	4,045,320	3,843,513
Building and Grounds	3,021,654	2,181,903
Grants	2,172,973	1,972,387
IT – Processing/Services/Equipment	2,604,459	2,251,608
Utilities	1,817,021	1,935,157
Travel	1,231,113	1,150,339
Loan Repayment – BND	1,135,547	
Professional Service/Supply/Material	1,013,737	828,765
Equipment	796,145	439,636
Repairs	707,514	588,445
Bond Payments / Special Assessments	653,822	658,535
Rent of Building Space	541,090	514,267
Inmate Wages	522,366	481,580
Supplies	404,628	452,469
Professional Development	185,746	195,397
Building Expansion / Extraordinary Repairs	127,434	3,404,286
Other Expenses	690,025	704,910
<b>Total Expenditures and Other Uses</b>	<b><u>\$106,674,326</u></b>	<b><u>\$102,005,701</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>
Accrued Leave Payments	\$ 4,639,529		\$ 4,639,529	\$ 535,440	\$ 4,104,089
Capital Construction Carryover		\$ 4,068,798	4,068,798	3,937,684	131,114
Adult Services	183,545,659	1,363,796	184,909,455	175,800,193	9,109,262
Youth Correctional Center	28,865,123	98,445	28,963,568	28,394,680	568,888
<b>Totals</b>	<u>\$217,050,311</u>	<u>\$ 5,531,039</u>	<u>\$222,581,350</u>	<u>\$208,667,997</u>	<u>\$ 13,913,353</u>
<b>Expenditures by Source:</b>					
General Fund	\$180,915,389	\$ 1,773,279	\$182,688,668	\$178,475,645	\$ 4,213,023
Other Funds	36,134,922	3,757,760	39,892,682	30,192,352	9,700,330
<b>Totals</b>	<u>\$217,050,311</u>	<u>\$ 5,531,039</u>	<u>\$222,581,350</u>	<u>\$208,667,997</u>	<u>\$ 13,913,353</u>

### Appropriation Adjustments:

The \$4,068,798 increase in the Capital Construction Carryover line was approved by the Construction Carryover Committee.

The \$1,363,796 increase in the Adult Services line consisted of the following adjustments:

- \$7,943 - authorized by House Bill 1015 of the 2013 Session Laws, section 11, for increased general fund spending authority for the state internship program.
- \$26,245 - authorized by House Bill 1015 of the 2013 Session Laws, section 8, for providing temporary employee health insurance adjustments for state employees determined to be full time.
- \$194,061 - authorized by House Bill 1015 of the 2013 Session Laws, section 6, and approved by the Emergency Commission to receive appropriation authority from the Energy Development Impact Funding Pool for employee housing rental assistance and temporary salary increases for employees affected by energy development.
- \$1,135,547 - authorized by Senate Bill 2023 of the 2015 Session Laws, section 1, to increase the general fund spending authority to be used for defraying the expenses of the Department of Corrections and Rehabilitation.

The \$98,445 increase in the Youth Correctional Center line consisted of the following adjustments:

- \$1,337 - authorized by House Bill 1015 of the 2013 Session Laws, section 11, for increased general fund spending authority for the state internship program.
- \$12,172 - authorized by House Bill 1015 of the 2013 Session Laws, section 8, for providing temporary employee health insurance adjustments for state employees determined to be full time.
- \$84,936 - authorized by House Bill 1015 of the 2013 Session Laws, section 6, and approved by the Emergency Commission to receive appropriation authority from the Energy Development Impact Funding Pool for employee housing rental assistance and temporary salary increases for employees affected by energy development.

**Expenditures Without Appropriations Of Specific Amounts:**

Insurance Recoveries Property Fund has a continuing appropriation authorized by NDCC section 54-44.1-09.1 (\$12,030 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 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 revenues for Adult Services and Youth Services.
- Controls surrounding the processing of expenditures for Adult Services and Youth Services.
- Controls surrounding purchases made using purchase cards.
- Controls effecting the safeguarding of pharmacy and Roughrider Industries inventory.
- Controls surrounding inmate accounts.
- Controls effecting the safeguarding of assets.
- Controls relating to compliance with legislative intent.
- Controls surrounding the ConnectND (PeopleSoft) system.
- Controls surrounding the Macola information system
- Controls surrounding changes to inmates' prison release dates.

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

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

Auditors are required to report deficiencies in internal control that are significant within the context of the objectives of the audit. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect (1) misstatements in financial or performance information, (2) violations of laws and regulations, or (3) impairments of effectiveness or efficiency of operations, on a timely basis. Considering both qualitative and quantitative factors, we identified the following significant deficiency in internal control. We also noted other matters involving internal control that we have reported to management of Department of Corrections and Rehabilitation in a management letter dated January 4, 2016.

## ***Lack of Controls Over Pharmacy Inventory (Finding 15-1)***

### **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 a 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.*

*Due to the fact the vendor of the existing electronic medical record (EMR) recently ceased business operations and is no longer providing EMR application support, the DOCR is in the process of securing the use of a correctional pharmacy software application from a different vendor. This application provides for a complete perpetual inventory system and is expected to be deployed and in use by the end of calendar year 2016. It is important to note that mitigating controls and proper segregation of duties surrounding the purchase, receipt, and disbursement of medications from pharmacy are and will continue to be in place.*

## *Compliance With Legislative Intent*

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In our audit for the biennium ended June 30, 2015, we identified and tested the 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:

- Conduct a land use study of the Missouri River Correctional Center site including options for relocating the facility. (Senate Bill 2015, section 4 of the 2013 Legislative Session).
- Compliance with the requirement to develop a prison population management plan and report on the plan annually to the budget section of the legislative management (Senate Bill 2015, section 6 of the 2013 Legislative Session).
- Established policies and procedures to ensure proper payments to crime victims (NDCC 54-23.4-06).
- Proper use of the following legally restricted funds:
  - Community Service Supervision fund.
  - Probationer Violation Transportation fund.
  - State Penitentiary Land fund.
  - Crime Victims Gift fund.
- Application of proper statutory rates relating to revenue.
- Proper authorization of the Department of Corrections and Rehabilitation's funds.
- Proper use of the State Treasurer (State Constitution, article X, section 12).
- Compliance with appropriations and related transfers (2013 North Dakota Session Laws chapter 46).
- 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* require auditors to report all instances of fraud and illegal acts unless they are inconsequential within the context of the audit objectives. Further, auditors are required to report significant violations of provisions of contracts or grant agreements, and significant abuse that has occurred or is likely to have occurred.

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



While we did not find any items that were required to be reported in accordance with *Government Auditing Standards*, we noted a certain inconsequential or insignificant instance of non-compliance that we have reported to management of the Department of Corrections and Rehabilitation in a management letter dated January 4, 2016.

## *Operations*

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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 certain matters involving operations that we have reported to management of the Department of Corrections and Rehabilitation in a management letter dated January 4, 2016.

## ***Prior Recommendations Not Implemented***

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

### **Lack of Controls Over Pharmacy Inventory (Finding 13-1)**

#### **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.
- Ensure there is proper segregation of duties surrounding the ordering of drugs.

#### **Status:**

Partially Implemented. See recommendation 15-1.

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

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January 4, 2016

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, 2015, 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 15-1: We recommend the North Dakota Youth Correctional Center reconcile the bank statements to the original receipts for the Juvenile Trust Fund account.

### **INVENTORY**

Informal Recommendation 15-2: We recommend the Rough Rider Industries Commissary keep evidence supporting their processes of properly reviewing adjustments made to inventory.

## LEGISLATIVE INTENT

Informal Recommendation 15-3: 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.

## PEOPLESOFT SYSTEM ACCESS

Informal Recommendation 15-4: We recommend the Department of Corrections and Rehabilitation ensure access privileges are properly restricted to those who need access to complete their job duties and to achieve proper segregation of duties.

## OPERATIONAL IMPROVEMENTS

Informal Recommendation 15-5: We recommend the Department of Corrections and Rehabilitation develop written policies and procedures surrounding:

- The inspection process at Correctional Facilities;
- Violation enforcement of Correctional Facilities; and
- Handling of Correctional Facility complaints.

Management of Department of Corrections and Rehabilitation 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,



Delan Hellman  
Auditor in-charge

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Division of State Audit

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