

NORTH DAKOTA STATE SEED DEPARTMENT

FARGO, NORTH DAKOTA

Audit Report

For the Two-year Period Ended
June 30, 2014

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
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BISMARCK, NORTH DAKOTA 58505

Transmittal Letter

June 22, 2015

The Honorable Jack Dalrymple, Governor
Members of the North Dakota Legislative Assembly
Members of the North Dakota State Seed Commission
Mr. Ken Bertsch, Commissioner, North Dakota State Seed Department

We are pleased to submit this audit of the North Dakota State Seed Department for the two-year period ended June 30, 2014. 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 Cory Wigdahl, CFE. Robyn Brenden and Travis Klinkhammer, CPA, were the staff auditors. Robyn Hoffmann, CPA, was the audit manager. Inquiries or comments relating to this audit may be directed to the audit manager by calling (701) 239-7291. We wish to express our appreciation to Commissioner Bertsch and his staff for the courtesy, cooperation, and assistance they provided to us during this audit.

Respectfully submitted,

A handwritten signature in dark ink, appearing to read "Rob Peterson", written over a horizontal line.

Robert R. Peterson
State Auditor

Executive Summary

Introduction

The Seed Department was established by the North Dakota Legislature in 1931 as the state's designated authority for all seed certification and regulatory matters. The Seed Department is unique by comparison to most state agencies, or seed certification entities, in that it is a self-funded agency of government, and provides inspection, testing, and regulatory enforcement services for all crops, including potatoes. A nine-member seed commission acts as a board of directors for the agency. Members are selected to serve by various agriculture industry organizations, including the North Dakota Crop Improvement Association, North Dakota Certified Seed Potato Growers Association, North Dakota Agricultural Association, Northern Plains Potato Growers Association, North Dakota Potato Council, North Dakota Grain Dealers Association, North Dakota Dry Edible Bean, Seed Growers Association, and the Director of the North Dakota State University Agriculture Experiment Station. The Commissioner of Agriculture, or his designee, serves as chairman of the Commission. The Commission appoints a State Seed Commissioner, who serves as chief executive officer of the Department.

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 North Dakota State Seed Department in accordance with generally accepted accounting principles so an opinion is not applicable. The agency's transactions were tested and included in the state's basic financial statements on which an unqualified opinion was issued.

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

Yes.

3. Was internal control adequate and functioning effectively?

Yes.

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

No.

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

Yes, the North Dakota State Seed Department has implemented 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 12 of this report, along with management's response, to two informal recommendations.

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.*

None.

9. *Identify any significant audit adjustments.*

None.

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, ConnectND Human Capital Management (HCM) and State Seed Administration Software (SSAS) are high-risk information technology systems critical to the North Dakota State Seed Department. No exceptions were noted that directly related to the operations of an informational technology system.

Audit Objectives, Scope, and Methodology

Audit Objectives

The objectives of this audit of the North Dakota State Seed Department for the two-year period ended June 30, 2014 were to provide reliable, audited financial statements and to answer the following questions:

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

Audit Scope

This audit of the North Dakota State Seed Department is for the two-year period ended June 30, 2014. 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 North Dakota State Seed Department has operations in the following locations. Each location was included in the audit scope:

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

Audit Methodology

To meet the objectives outlined above, we:

- Prepared financial statements from the legal balances on the state's accounting system tested as part of this audit and the audit of the state's Comprehensive Annual Financial Report and developed a discussion and analysis of the financial statements.
- Performed detailed analytical procedures including computer-assisted auditing techniques. These procedures were used to identify high-risk transactions and potential problem areas for additional testing.
- Tested internal control and compliance with laws and regulations which included selecting representative samples to determine if controls were operating effectively and to determine if laws were being followed consistently. 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 North Dakota State Seed Department's processes and procedures.

In aggregate there were no significant limitations or uncertainties related to our overall assessment of the sufficiency and appropriateness of audit evidence.

Discussion and Analysis

The accompanying financial statements have been prepared to present the North Dakota State Seed Department's revenues and expenditures on the legal (budget) basis. The accompanying financial statements are not intended to be presented in accordance with generally accepted accounting principles (GAAP).

For the two-year period June 30, 2014, operations of the North Dakota State Seed Department were primarily supported by regulatory fees.

Financial Summary

Revenues consisted primarily of regulatory fees. Other revenues during the audited period included fees for service and federal grant funds. These all remained fairly constant for the North Dakota State Seed Department, except regulatory fees which increased by approximately \$353,000. This was primarily due to the late planting season during 2013, thus postponing planting and seed certifications into fiscal year 2014. Total revenues were \$2,947,314 for the year ended June 30, 2014 as compared to \$2,553,652 for the year ended June 30, 2013.

Total expenditures for the North Dakota State Seed Department were \$2,676,868 for the year ended June 30, 2014 as compared to \$2,567,199 for the prior year. Expenditures remained fairly constant for the North Dakota State Seed Department, increasing only slightly.

Analysis of Significant Changes in Operations

There were no significant changes in operations.

Analysis of Significant Variances - Budgeted and Actual Expenditures

For the fiscal years ended June 30, 2014 and 2013, there were no significant variances between the original and final budgeted amounts or between the final budgeted and actual expenditures.

Financial Statements

Statement of Revenues and Expenditures

Revenues and Other Sources:	June 30, 2014	June 30, 2013
Regulatory & Inspection Fees	\$ 2,752,346	\$ 2,399,229
Fees for Services	93,906	108,537
Federal Grants	81,331	24,903
Licenses, Permits, & Fees	6,629	6,625
Interest & Investment Earnings	5,833	7,794
Leases, Rents, and Royalties	5,720	5,720
Miscellaneous Revenue	1,549	844
Total Revenues and Other Sources	\$ 2,947,314	\$ 2,553,652
Expenditures and Other Uses:		
Salaries and Benefits	\$ 1,882,307	\$ 1,836,510
Travel	154,089	167,553
Fees - Professional Services	123,291	58,195
Utilities	103,078	90,867
Grants, Benefits & Claims	70,000	70,000
Operating Fees and Services	47,403	29,543
Repairs	46,007	11,694
Supply/Material-Professional	36,244	21,830
Lab Supplies	33,014	32,850
Office Supplies	26,309	10,844
Bldg, Grounds, Vehicle Supply	23,079	9,520
Postage	21,604	23,816
Professional Development	21,603	25,405
Printing	18,666	14,142
IT Contractual Services and Repairs	17,957	19,196
IT-Communications	14,658	14,790
Rentals/Leases-Equip & Other	11,038	10,946
Insurance	8,029	8,707
IT - Data Processing	5,887	5,177
Supplies - IT Software	5,775	9,037
Other Equipment Under \$5,000	3,816	7,150
IT Equip Under \$5000	2,768	
Office Equip and Furniture Under \$5,000	239	
Miscellaneous Supplies	6	
IT Equip/Software Over \$5000		89,426
Total Expenditures and Other Uses	\$ 2,676,868	\$ 2,567,199

Statement of Appropriations

	Original Appropriation	Current Appropriation	Expenditures	Remaining Appropriation
Seed Operations	\$ 6,894,011	\$ 6,894,011	\$ 5,052,164	\$ 1,841,847
Totals	\$ 6,894,011	\$ 6,894,011	\$ 5,052,164	\$ 1,841,847
Expenditures by Source:				
Special Funds	\$ 6,894,011	\$ 6,894,011	\$ 5,052,164	\$ 1,841,847
Totals	\$ 6,894,011	\$ 6,894,011	\$ 5,052,164	\$ 1,841,847

As of the beginning of fiscal year 2014, the North Dakota State Seed Department no longer has an appropriated budget, thus for the year ended June 30, 2014, there are no appropriations to report.

Internal Control

In our audit for the two-year period ended June 30, 2014, we identified the following areas of the North Dakota State Seed Department's internal control as being the highest risk:

Internal Controls Subjected to Testing:

- Controls surrounding the processing of revenues.
- Controls surrounding the processing of expenditures.
- Controls effecting the safeguarding of assets.
- Controls relating to compliance with legislative intent
- Controls surrounding the ConnectND (PeopleSoft) system.
- Controls surrounding the State Seed Administrative Software

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

We gained an understanding of internal control surrounding these areas and concluded as to the adequacy of their design. We also tested the operating effectiveness of those controls we considered necessary based on our assessment of audit risk. We concluded 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 other matters involving internal control that we have reported to management of the North Dakota State Seed Department in a management letter dated June 22, 2015.

Compliance With Legislative Intent

In our audit for the two-year period ended June 30, 2014, we identified and tested the North Dakota State Seed Department's compliance with legislative intent for the following areas we determined to be significant and of higher risk of noncompliance:

- Members of the Seed Commission received \$135/day and reimbursement for expenses (NDCC 4.1-52-06).
- The Seed Commission appointed a Commissioner and fixed the salary within legislative appropriation (NDCC 4.1-52-08).
- The Commissioner, with the approval of the Seed Commission, established and charged fees for laboratory tests and services (NDCC 4.1-52-10).
- The Commissioner established a seed certification system, and made the requirements for seed certification readily available in electronic and printed formats (NDCC 4.1-53-42).
- Nonresidents are required to submit an annual application for a nonresident seed dealer license and submit an annual license fee (NDCC 4.1-53-41).
- Proper use of the State Treasurer (State Constitution, article X, section 12).
- Compliance with appropriations and related transfers (2011 and 2013 North Dakota Session Laws).
- Compliance with OMB's Purchasing Procedures Manual.
- Travel-related expenditures are made in accordance with OMB policy and state statute.
- Proper use of outside bank accounts, petty cash funds, and proper authority for investments outside the Bank of North Dakota.
- 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.

Management Letter (Informal Recommendations)

June 22, 2015

Mr. Ken Bertsch
State Seed Commissioner
North Dakota State Seed Department
P.O. Box 5257
Fargo, ND 58105-5257

Dear Mr. Bertsch:

We have performed an audit of the North Dakota State Seed Department for the two-year period ended June 30, 2014, and have issued a report thereon. As part of our audit, we gained an understanding of the North Dakota State Seed Department'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 state 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.

Security Access

Condition:

We noted three users within the State Seed Administration Software (SSAS) with full administrative access, besides the administrator user account; two of which are the programming consultants, and the other is the Administrative Officer. Since the Administrative Officer is responsible for entering and posting payments to customer's accounts within the SSAS, having the ability to change anything in the SSAS is cause for concern.

Criteria:

Proper internal controls should provide reasonable assurance that operations are effective and efficient and financial reporting is reliable. An integral part of operational effectiveness and efficiency as well as ensuring the reliability of financial information is requiring that proper restrictions are placed on the different levels of access.

Effect:

By not limiting the administrative access to the programming consultants, it could lead to unauthorized changes, affecting the financial statements.

Cause:

Per discussion with the Administrative Officer, administrative access is necessary to troubleshoot the SSAS to help keep consulting/programming costs down.

Informal Recommendation 14-1:

We recommend the North Dakota State Seed Department restrict the administrative level of access to the programming consultants.

North Dakota State Seed Response/Planned Corrective Action:

Disagree. The programming consultants involved with SASS are utilized only for development/programming of software. SSAS is not a general ledger program; it is primarily a tracking and reporting program with an accounts receivable integration. SASS impacts only revenues and accounts receivable and is not integrated with PeopleSoft. The software is completely table driven to allow flexibility and decrease costs for re-programming. It was intended to provide a robust, flexible efficient tool to accommodate changing business needs.

Modification of setup files is an operations function rather than a programming function intentionally. Our consultants/programmers are not available to us for the purpose of operations; their availability is limited to programming only. Set-up files, which also contain financial data, are often modified daily to allow for changes in varieties, crops, required tests, inspection types, file locations, auto-numbering, default printers, web data transfer, form printing, staff additions and removals, etc.

Unfortunately, in a Department our size, our Administrative Officer serves the role of our lead IT person as well as our accountant. We do not have any additional IT personnel on staff. Limiting access would not be efficient or effective. Hiring an additional staff member for this purpose would not be cost effective.

All fees charged are independently and consistently reviewed by other Department staff in the process of daily customer reporting. Every credit to accounts receivable is fully supported and approved by the Seed Commissioner, as was proven in your 100% examination. Security access to SASS has been reviewed without any recommendations in our audits since 2009.

Auditor Concluding Remarks:

We stand by our recommendation to limit the full administrative access to the programming consultants, since the SSAS is a significant subsidiary ledger that accounts for, at minimum, 93% of North Dakota State Seed Department's revenue, and maintains the details of customer billings, receipts, and accounts receivable. Furthermore, we did not perform a 100% examination of accounts receivable, we performed a sample of accounts receivable.

Remittance Listing

Condition:

We noted checks are being restrictively endorsed as the mail is being opened; however, there is no remittance listing prepared documenting monies received.

Criteria:

Committee of Sponsoring Organizations (COSO) of the Treadway Commission publication Internal Control - Integrated Framework: Proper design and implementation of internal control policies and procedures for performance measures, segregation of duties, approval, monitoring, and verification methods are necessary to ensure objectives are effectively achieved.

Effect:

With no remittance listing prepared and verified, the North Dakota State Seed Department lacks the assurance that all checks and cash may not be accounted for and deposited, increasing the potential risk of fraud, waste, abuse.

Cause:

A remittance listing is not prepared because the North Dakota State Seed Department does not deposit checks where the customer is overpaying and checks that are for applications are not deposited until the application is reviewed and approved - in both of these instances the checks are restrictively endorsed.

Informal Recommendation 14-2:

We recommend the North Dakota State Seed Department prepare a remittance listing to include all monies to be deposited - cash and checks. We further recommend that the remittance listing is signed/initialed and dated by the person preparing the remittance listing, and that there is a documented verification that the remittance listing agrees to the daily posting of payments to customer's accounts and the daily deposit.

North Dakota State Seed Response/Planned Corrective Action:

Disagree. This informal recommendation is nearly identical to one included in our 2011 audit. After the auditors did an in-depth review during their 2013 audit, this recommendation was removed. We have not made any changes to our processes, procedures or personnel during the entire period, and are unaware of what has changed to cause this recommendation to be included again. Our position remains the same as that written in the 2011 response.

Auditor Concluding Remarks:

We stand by our recommendation that the North Dakota State Seed Department prepare a remittance listing. Currently, the North Dakota State Seed Department does not prepare a remittance listing, but rather prints out a list of payments posted to customer's accounts, leaving checks and cash not posted to customer's accounts and not deposited potentially subject to loss or theft.

I encourage you to call myself at 701-239-7296 or the audit manager at 701-239-7291 if you have any questions about the implementation of recommendations included in this letter.

Sincerely,



Cory Wigdahl, CFE
Auditor in-charge

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