

September 2003

LEGISLATIVE AUDIT AND FISCAL REVIEW COMMITTEE - STATUTORY DUTIES AND RESPONSIBILITIES FOR THE 2003-04 INTERIM - RECOMMENDATIONS AND REQUESTS MADE DURING PREVIOUS INTERIMS

The Legislative Council by law appoints a Legislative Audit and Fiscal Review Committee as a division of its Budget Section. Pursuant to North Dakota Century Code (NDCC) Section 54-35-02.1, the committee is created:

- For the purpose of studying and reviewing the financial transactions of the state.
- To assure the collection of revenues and the expenditure of money in compliance with law, legislative intent, and sound financial practices.
- To provide the Legislative Assembly with formal, objective information on revenue collections and expenditures as a basis for legislative action to improve the fiscal structure and transactions of the state.

STATUTORY DUTIES AND RESPONSIBILITIES

The committee is charged by statute with the following duties and responsibilities for the 2003-05 biennium:

1. **State Fair Association** - Receive annual audit reports from the State Fair Association, pursuant to NDCC Section 4-02.1-18.
2. **Ethyl alcohol and methanol producers** - Receive annual audit reports from any corporation that produces agricultural ethyl alcohol or methanol in this state and which receives a production subsidy from the state, pursuant to NDCC Section 10-19.1-152, receive annual audit reports from any limited liability company that produces agricultural ethyl alcohol or methanol in this state and which receives a production subsidy from the state, pursuant to Section 10-32-156, and receive annual audit reports from any limited partnership that produces agricultural ethyl alcohol or methanol in this state and which receives a production subsidy from the state, pursuant to Section 45-10.1-71.
3. **Department of Human Services accounts receivable** - Receive annual reports on the status of accounts receivable for the Department of Human Services and Developmental Center at Westwood Park, Grafton, pursuant to NDCC Sections 25-04-17 and 50-06.3-08.

4. **Low-risk incentive fund** - Receive annual audit reports and economic impact reports from the North Dakota low-risk incentive fund. North Dakota Century Code Section 26.1-50-05 provides for the audit report to be submitted to the Legislative Council, which has assigned the responsibility to this committee.
5. **Stockmen's Association** - Receive a biennial audit report from the North Dakota Stockmen's Association. North Dakota Century Code Section 36-22-09 provides for the audit report to be submitted to the Legislative Council. The Legislative Council assigned the responsibility to this committee.
6. **Job Service North Dakota** - Receive the biennial performance audit report for the divisions of Job Service North Dakota, pursuant to NDCC Section 52-02-18.
7. **Performance audits** - The State Auditor is to conduct or provide for performance audits of state agencies as determined necessary by the State Auditor or this committee, and the State Auditor must obtain approval from this committee prior to hiring a consultant to assist with conducting a performance audit, pursuant to NDCC Section 54-10-01.
8. **Frequency of audits** - Determine the frequency of audits or reviews of state agencies, pursuant to NDCC Section 54-10-01.
9. **Political subdivisions** - Determine if the State Auditor is to perform audits of political subdivisions on a more frequent basis than once every two years, pursuant to NDCC Section 54-10-13, and direct the State Auditor to audit or review the accounts of any political subdivision, pursuant to Section 54-10-15.
10. **Study and review audit reports** - Pursuant to NDCC Section 54-35-02.2, the committee is charged with the following responsibilities:
 - a. To study and review audit reports selected by the committee from those submitted by the State Auditor.
 - b. To confer with the State Auditor regarding the audit reports reviewed by the committee.

- c. As necessary, to confer with representatives of state departments, agencies, and institutions audited in order to obtain information regarding fiscal transactions and governmental operations.
- 11. **Workforce Safety and Insurance** - Receive annual reports from the director of Workforce Safety and Insurance and the chairman of the Workforce Safety and Insurance Board of Directors, pursuant to NDCC Section 65-02-03.3, and receive reports from the director of Workforce Safety and Insurance, the chairman of the Workforce Safety and Insurance Board of Directors, and the auditor regarding the biennial performance audit of Workforce Safety and Insurance, pursuant to Section 65-02-30.
- 12. **Information Technology Department** - Receive annual reports on state information technology projects and plans, pursuant to NDCC Section 54-59-19.

REQUESTS AND RECOMMENDATIONS DURING PREVIOUS INTERIMS

The committee has made various recommendations and requests during past interims, including:

1. **Discussion of audit findings prior to presentation of report** - The State Auditor should consider discussing audit findings with appropriate boards or commissions prior to the audit report being presented to the committee.
2. **Actions taken by audited agency** - Audited agencies, boards, and commissions should report to the committee at the time the audit report is presented regarding any actions taken as a result of audit findings contained in the report.
3. **Implementation of recommendations** - Each state agency and institution should comply with and implement, within the limits of the law, recommendations contained in audit reports prepared by the State Auditor's office. Such compliance and implementation should be viewed toward improvement of government operations, including fiscal operations and to full execution of the law.
4. **Six-month review** - The State Auditor's office should determine whether agencies have complied with the auditor's recommendations within six months after a report has been accepted by this committee; the State Auditor should report to this committee, or another appropriate legislative committee, regarding any recommendations not implemented.
5. **Response to recommendations** - Each audit report prepared by the State Auditor should include a summary of audit recommendations, along with the audited agency's written response to the recommendations. The summary is to be in recommendation-response format.
6. **Copies of management letters** - The State Auditor should provide copies of management letters to committee members.
7. **Use of salaries and wages funding** - The State Auditor should consider including in audit reports information on the amount of salaries and wages funding spent on filled full-time equivalent (FTE) positions and the amount relating to vacant FTE positions which is spent for other purposes.
8. **Report on significant findings and recommendations** - The State Auditor should consider providing a report to the Appropriations Committees and each member of the Legislative Audit and Fiscal Review Committee at the beginning of each legislative session regarding significant audit findings and recommendations contained in the financial and performance audit reports presented to the Legislative Audit and Fiscal Review Committee during the previous interim.

AUDIT GUIDELINES

The committee has developed guidelines for audits performed by the State Auditor's office and independent certified public accountants. The guidelines require that audit reports include specific statements and recommendations regarding:

1. Whether expenditures are made in accordance with legislative appropriations and other state fiscal requirements and restrictions.
2. Whether revenues are accounted for properly.
3. Whether financial controls and procedures are adequate.
4. Whether the system of internal control is adequate and functioning effectively.
5. Whether financial records and reports reconcile with those of state fiscal offices.
6. Whether there is compliance with statutes, laws, rules, and regulations under which the agency was created and is functioning.
7. Whether there is evidence of fraud or dishonesty.
8. Whether there are indications of inefficiency in financial operations and management of the agency.
9. Whether actions have been taken by agency officials with respect to findings and recommendations set forth in the audit reports for preceding periods.

10. Whether all activities of the agency are encompassed within appropriations of specific amounts.
11. Whether the agency has implemented the statewide accounting and management information system, including the cost-allocation system.
12. Whether the agency develops a budget of anticipated expenditures and revenues and compares, on at least a quarterly basis, budgeted expenditures and revenues to actual expenditures and revenues accounted for using the accrual basis of accounting.

NEW AUDIT APPROACH

During the 1999-2000 interim the committee received testimony from a representative of the State Auditor's office regarding the agency's plan to change the audit approach used in conducting audits of state agencies and institutions. For audits of state agencies and institutions conducted by the State Auditor's office, governmental auditing standards for performance audits are more applicable than governmental auditing standards for financial audits. A report on an audit conducted using performance auditing standards includes audited financial statements but does not include an opinion on those financial statements because the audit will not determine if the financial statements are prepared in accordance with generally accepted accounting principles. The committee supported the proposal presented by the State Auditor's office to begin conducting audits of state agencies and institutions using governmental auditing standards for performance audits.

The State Auditor's office began to use the new audit approach during the 2001-02 interim. Financial audits conducted by public accounting firms continue to utilize governmental auditing standards for financial audits.

COMPONENT UNITS OF STATE INSTITUTIONS

During the 2001-02 interim the committee received testimony from a representative of the North Dakota University System regarding the State Board of Higher Education's process for reviewing and approving proposed agreements for the establishment of a component unit and the status of existing component units located on North Dakota University System property. The State Auditor's office and the University System agreed to follow four guidelines to provide for the proper financial reporting of University System component units, summarized as follows:

- I. The University System will evaluate any proposed component unit to ensure compliance with generally accepted accounting

principles relating to reporting and disclosure. The University System will submit to the State Auditor's office the campus's decision regarding proper reporting and disclosure, substantiating documentation, a memorandum outlining the intended financial statement treatment of the component unit, articles of incorporation, corporate bylaws, Internal Revenue Service Form 990, and a listing of board members.

- II. The State Auditor's office will review the information provided by the University System to determine an entity's proper reporting status. If necessary, the State Auditor will consult with the Attorney General's office. Representatives of the State Auditor's office and the University System will meet to discuss any differences in the determination of the proper reporting status.
- III. The component unit, once established, may contract with a public accounting firm to perform an annual financial audit, a copy of which must be submitted to the State Auditor's office. If necessary to determine the relationship between the component unit and the university, the State Auditor's office will have access to the board minutes of the component unit as the minutes relate to business conducted between the component unit and the university. In addition, the component unit will contract with an independent auditor to provide written confirmation that minutes provided to the State Auditor's office include all information required to be disclosed in the university audit report relating to transactions or relationships between the component unit and the college or university.
- IV. Information contained in the board minutes reviewed by the State Auditor's office will be subject to NDCC Section 54-10-22.1 regarding confidentiality. Any information in the board minutes which does not relate to transactions or relationships between the university and the component unit will not be included in the working papers of the State Auditor's office and therefore will not be available for public inspection.

DRAFT AUDIT REPORTS

During the 2001-02 interim the committee received testimony from a representative of the State Auditor's office regarding the confidentiality of draft audit reports. Draft audit reports are exempt from open records law; however, once the draft is released to an agency for comment, the exemption is lost. House Bill No. 1051, as approved by the 2003 Legislative Assembly, amends NDCC Section 54-10-26 and provides that a

draft audit report of the State Auditor released to the governing body or management of an audited entity is confidential until the final audit report is issued or work ceases on the audit. The bill also provides that working papers, which are exempt from open records requirements, include draft audit reports.

PERFORMANCE AUDITS

During the 2001-02 interim the committee received performance audit reports on the service payments for elderly and disabled (SPED) and expanded SPED programs, the Veterans Home, Job Service North Dakota, and the Workers Compensation Bureau.

In addition to performance audits required by law or requested by the committee, the State Auditor's office was directed by the 2003 Legislative Assembly to conduct a performance audit of the Department of

Veterans Affairs and Administrative Committee on Veterans Affairs (House Bill No. 1007) and the Department of Corrections and Rehabilitation (House Bill No. 1506). The State Auditor's office indicated the performance audits of the Department of Transportation's Motor Vehicle and Drivers License Division, Department of Veterans Affairs, Administrative Committee on Veterans Affairs, and Department of Corrections and Rehabilitation will be available for presentation to the committee during the 2003-04 interim. In addition, followup reports on the Department of Human Services child support enforcement, SPED, and expanded SPED will be completed during the interim.

The following table lists the status of performance audits presented to the Legislative Audit and Fiscal Review Committee during the 1997-99, 1999-2001, and 2001-03 bienniums:

Performance Audit	Status
1997-99 biennium	
State procurement practices	Presented October 7, 1997, and January 21, 1998
State employee classification system	Presented October 6, 1998, and January 27, 1999
Workers Compensation Bureau	Presented October 6, 1998
Job Service North Dakota	Presented October 6, 1998
1999-2001 biennium	
Contracts for services	Presented May 22-23, 2000
Child support enforcement program (Department of Human Services)	Presented October 16-17, 2000
Workers Compensation Bureau	Presented October 16-17, 2000
Job Service North Dakota	Presented October 16-17, 2000
2001-03 biennium	
Aging services, SPED, and expanded SPED programs (Department of Human Services)	Presented November 26, 2001
Veterans Home	Presented October 2, 2002, and January 22, 2003
Workers Compensation Bureau	Presented October 2, 2002
Job Service North Dakota	Presented October 2, 2002