



FINANCIAL AUDIT DIVISION REPORT

**Department of Agriculture
(including the Rural Finance Authority)**

**Internal Controls and
Compliance Audit**

July 2012 through March 2015

January 28, 2016

Report 16-01

FINANCIAL AUDIT DIVISION
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The Financial Audit Division annually audits the state's financial statements and, on a rotating schedule, audits agencies in the executive and judicial branches of state government, three metropolitan agencies, and several "semi-state" organizations. The division has a staff of about 30 auditors, most of whom are CPAs. The division conducts audits in accordance with standards established by the American Institute of Certified Public Accountants and the Comptroller General of the United States.

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Conclusion on Internal Controls

The Financial Audit Division bases its conclusion about an organization's internal controls on the number and nature of the control weaknesses we found in the audit. The three possible conclusions are as follows:

Conclusion	Characteristics
Adequate	The organization designed and implemented internal controls that effectively managed the risks related to its financial operations.
Generally Adequate	With some exceptions, the organization designed and implemented internal controls that effectively managed the risks related to its financial operations.
Not Adequate	The organization had significant weaknesses in the design and/or implementation of its internal controls and, as a result, the organization was unable to effectively manage the risks related to its financial operations.



January 28, 2016

Representative Sondra Erickson, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

David Frederickson, Chair
Rural Finance Authority

Members of the Rural Finance Authority Board

David Frederickson, Commissioner
Department of Agriculture

This report presents the results of our internal controls and compliance audit of the Department of Agriculture, including the Rural Finance Authority, for the period from July 1, 2012, through March 31, 2015. The objectives of this audit were to determine if the department had adequate internal controls for its financial operations and complied with finance-related legal requirements.

We discussed the results of the audit with the office's staff at an exit conference on January 13, 2016. This audit was conducted by Scott Tjomsland, CPA, CISA (Audit Director) and auditors Emily Wiant, Jennyfer Hildre, and Heather Varez, CPA.

We received the full cooperation of the department's staff while performing this audit.

Handwritten signature of James R. Nobles in black ink.

James R. Nobles
Legislative Auditor

Handwritten signature of Cecile M. Ferkul in black ink.

Cecile M. Ferkul, CPA, CISA
Deputy Legislative Auditor

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Report Summary

The Department of Agriculture serves as the state's major agricultural regulatory and promotional agency. The department provides a diverse range of services to Minnesota farmers, consumers, and the agricultural community, including education, licensing and inspections, grants, and loans.

The Rural Finance Authority is a separate, public body whose purpose is to make credit available to farmers. The Department of Agriculture administers the authority's financial activity, including its loan programs.

We examined the department's internal controls over its financial operations and its compliance with finance-related legal requirements during the period from July 2012 through March 2015. Our review included revenue from various license, registration, and inspection fees and expenses related to payroll and employee business expense reimbursements. In addition, we reviewed financial activities related to the department's and the Rural Finance Authority's loan programs.

Conclusion

The Department of Agriculture's internal controls were generally adequate and, for the items we tested, generally complied with significant finance-related legal requirements; however, the department had some weaknesses in receipts and payroll.

Findings

- The Department of Agriculture undercharged registrants of nonagricultural pesticides for annual registration fees ([Finding 1, page 7](#)).
 - The Department of Agriculture did not adequately monitor and review timesheet data recorded by employees in the state's payroll system ([Finding 2, page 8](#)).
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Overview

Department of Agriculture

The Department of Agriculture serves as the state's major agricultural regulatory and promotional agency. Its mission is to enhance Minnesotans' quality of life by ensuring the integrity of our food supply, the health and strength of our environment, and the strength of our agricultural economy.

The department provides a diverse range of services directed to Minnesota farmers, consumers, and the agricultural community. Its activities include regulating pesticides and fertilizers, inspecting and certifying plant commodities, detecting and managing plant pests, and regulating and inspecting dairy, meat, and food products. The department also provides education and promotes Minnesota agricultural products through a variety of initiatives, including maintaining the Minnesota Grown Directory.

The department collected various dedicated receipts used to finance its licensing, inspection, regulatory, and registration activities. In addition, the department received General Fund appropriations totaling approximately \$24 million in fiscal year 2013 and \$32 million each year in fiscal years 2014 and 2015 to fund its operations and grants. Table 1 summarizes the department's total revenue and expenditures for fiscal years 2013 through 2015.

Table 1
Revenue and Expenditures
July 2012 through June 2015 (by Fiscal Year)

	<u>FY 2013</u>	<u>FY 2014</u>	<u>FY 2015¹</u>
Revenue:			
Fees and Other Receipts	\$32,070,741	\$32,281,993	\$34,615,950
Loan Repayments and Interest ²	32,207,679	21,775,510	19,847,545
Grants	<u>5,816,448</u>	<u>7,588,406</u>	<u>7,200,071</u>
Total Revenue	<u>\$70,094,868</u>	<u>\$61,645,909</u>	<u>\$61,663,566</u>
Expenditures:			
Payroll	\$33,824,597	\$34,331,176	\$36,447,626
Expense Reimbursements	508,441	522,422	581,482
Travel	1,573,271	1,433,144	1,389,986
Loans ³	20,005,883	15,433,515	14,335,933
Purchased Services	12,204,718	13,544,208	15,741,590
Grants, Aids, and Subsidies	8,464,484	7,902,591	11,267,175
Supplies/Equipment	1,471,807	1,246,586	1,414,514
Other Expenditures ⁴	<u>9,531,845</u>	<u>8,108,913</u>	<u>8,776,069</u>
Total Expenditures	<u>\$87,585,046</u>	<u>\$82,522,555</u>	<u>\$89,954,375</u>

¹This table includes fiscal year 2015 financial activity through June 30, 2015; however, the scope of our audit included fiscal year 2015 activity through March 2015.

² Loan repayments and interest included \$36,852,236 collected during fiscal years 2013 through 2015 for loan programs administered by the Rural Finance Authority.

³ Loans included \$26,332,658 disbursed during fiscal years 2013 through 2015 through loan programs administered by the Rural Finance Authority.

⁴Other expenditures included various services and agency and statewide indirect costs.

Source: State of Minnesota's accounting system.

Loan Programs

The department operates a variety of loan programs to assist farmers in developing and expanding their operations both directly through the agency and through the Rural Finance Authority. The department manages the Agricultural Best Management Practices Program, a water quality program in which the department makes no interest loans to local governments. The local governments, in turn, provide low interest loans to farmers and other producers for projects aimed at reducing water quality problems.

Rural Finance Authority

The Rural Finance Authority is a separate, public body whose purpose is to make credit available to farmers on terms and conditions not otherwise available from other credit sources. As set forth in *Minnesota Statutes 2015*, 41B.025, the board of the Rural Finance Authority consists of the commissioners of departments of Agriculture, Commerce, Employment and Economic Development, Management and Budget; the State Auditor; and six public members appointed by the Governor. The Rural Finance Authority's financial activity is administered by the Department of Agriculture.

The Rural Finance Authority manages several loan programs for a variety of purposes, including loans to assist beginning farmers to purchase land, loans for agricultural improvements, livestock expansion, livestock equipment, and disaster recovery. It makes credit available to farmers by partnering with private lenders and purchasing participating interests in loans. The Rural Finance Authority charges lower interest rates on its portion of the loans, making credit more affordable.

Objective, Scope, and Methodology

The objective of our audit of the Department of Agriculture was to answer the following questions for the period from July 1, 2012, through March 31, 2015:

- Were the department's internal controls adequate to ensure that it safeguarded its financial resources, accurately paid employees and vendors in accordance with management's authorizations, complied with finance-related legal provisions, properly administered the financial activities of the Rural Finance Authority, and created reliable financial data?
- Did the department comply with significant finance-related legal requirements?

To answer these questions, we gained an understanding of the department's financial policies and procedures. We considered the risk of errors in the

accounting records and potential noncompliance with relevant legal requirements. We analyzed accounting data to identify unusual trends or significant changes in financial operations. We examined samples of financial transactions and reviewed supporting documentation to test whether the department's controls were effective and if the transactions complied with laws, regulations, policies, and grant and contract provisions.

We conducted the audit in accordance with generally accepted government auditing standards applicable to performance audits. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusion based on our audit objectives.

We used various criteria to evaluate internal control and compliance. We used, as our criteria to evaluate the department's controls, the guidance contained in the *Standards for Internal Control in the Federal Government*, published by the U.S. Government Accountability Office.¹ We used state and federal laws, regulations, and contracts, as well as policies and procedures established by the department as evaluation criteria over compliance.

Conclusion

The Department of Agriculture's internal controls were generally adequate and, for the items we tested, generally complied with significant finance-related legal requirements; however, the department had some weaknesses in receipts and payroll.

The following *Findings and Recommendations* provide further explanation about the exceptions noted above.

¹ The state has adopted these standards as its internal control framework for the executive branch.

Findings and Recommendations

Finding 1

The Department of Agriculture undercharged registrants of nonagricultural pesticides for annual registration fees.

The department undercharged registrants of nonagricultural pesticides by up to \$350 annually for each nonagricultural pesticide registered.

Minnesota Statutes 2015, 18B.26, subd. 3, states:

...registrant shall pay a minimum annual registration application fee for each nonagricultural pesticide of \$350.... The registrant... shall pay, in addition to the \$350 minimum fee, a fee of 0.5 percent of annual gross sales of the nonagricultural pesticide....

Department staff believed that the \$350 fee was a minimum fee based on the percent of annual gross sales. The department appropriately required registrants to pay the initial \$350 fee, but it instructed registrants to exclude \$70,000 from the annual gross sales reported for each nonagricultural pesticide before calculating the fee owed based on annual gross sales.²

As a result, the department did not require registrants to pay a fee based on a percent of annual gross sales for any nonagricultural pesticide that had less than \$70,000 in annual gross sales. It also undercharged registrants reporting \$70,000 or more in annual gross sales by \$350 for each nonagricultural pesticide registered. We estimated the total amount undercharged for the audit period to be about \$100,000.

Recommendation

- *The Department of Agriculture should require registrants of nonagricultural pesticides to pay an annual gross sales fee equal to 0.5 percent of the total annual gross sales for each nonagricultural pesticide registered. Alternatively, the department could work with the Legislature to revise the statutory requirement to be consistent with the department's practice.*

² The required fee based on annual gross sales of \$70,000 is equal to \$350.

Finding 2

The Department of Agriculture did not adequately monitor and review timesheet data recorded by employees in the state's payroll system.

The department did not review two key payroll reports, (1) the payroll posting audit trail report and (2) the self service time entry audit report. Department employees generally used the state's automated self service time entry system to enter and authorize payroll hours.³ Once supervisors reviewed and approved employees' time, the hours were uploaded to the state's payroll system.

The payroll posting audit trail report is designed to ensure that employees were paid from the correct funding source. It shows the accounts to which each employee's payroll costs are charged.

Department of Management and Budget Policy PAY0028 requires agency accounting staff or program managers to do the following:

Document the review of the Payroll Posting Audit Trail each pay period to verify that employees have been charged to the correct account. This can be done on a sample basis or a detail basis.

The department also did not document its review of the self service time entry audit report, which is designed to ensure the accuracy and authorization of hours employees reported in the state's automated time reporting system. The report provides a list of employees that did not personally complete their time entry or whose time entry was approved by a backup approver.

Department of Management and Budget Policy PAY0017 states:

The best control over the integrity of employees' payroll information is achieved when employees prepare their own timesheets and supervisors, who have direct knowledge of employees' work, review and approve timesheets.

Use of backup approvers and payroll staff to modify or approve employee timesheets is permitted, but should be strictly limited. When backup approvers and payroll staff modify or approve timesheets, they should document the reason for the modification or approval... and notify the primary supervisor/manager to ensure that the timesheet modification or approval was appropriate.

The policy requires payroll staff to do the following:

³ During the audit period, employees in the Lab Services Division did not use the self service time entry system to record their time. These employees recorded their time in a separate system and submitted paper timesheets. Once supervisors approved the timesheets, they were forwarded to the payroll clerk who recorded the hours in the state's payroll system.

Complete a comprehensive review of the report each pay period. If a comprehensive review is not possible, review a representative sample each pay period. A comprehensive review must be completed on a quarterly basis. Audited sections or samples from the report must be kept with documented explanations.

Although department employees told us they reviewed this report, the employees did not document their review and did not always obtain explanations of why employees did not complete their own time entry, or why a backup approver approved the time.

In addition, the department assigned one employee as a backup approver for the employee's own timesheet. Department of Management and Budget policy PAY0017 states, "Employees should not approve their own timesheets." Being assigned as a backup approver gave this employee the ability to approve her own time. We reviewed all of the timesheets for this employee and did not identify any instances where the employee approved her own timesheet.

Recommendations

- *The Department of Agriculture should review and document the review of payroll system audit reports in compliance with state policies.*
 - *The Department of Agriculture should review its self service time entry approval assignments and eliminate the ability for employees (as approvers or backup approvers) to approve their own timesheets.*
-

January 21, 2016

James R. Nobles, Legislative Auditor
Office of the Legislative Auditor
Centennial Building, Room 140
658 Cedar Street
St. Paul, MN 55155

Dear Mr. Nobles,

Thank you for the opportunity to review and respond to your office's internal control and compliance audit of the Department of Agriculture. We value the professional review your staff has provided us with and appreciate the recommendations for improvement that have resulted.

Specific responses to the audit findings follow.

Finding 1: The Department undercharged registrants of nonagricultural pesticides by up to \$350 annually for each nonagricultural pesticide registered.

Audit Recommendation:

The Department of Agriculture should require registrants of nonagricultural pesticides to pay an annual gross sales fee equal to 0.5 percent of the total annual gross sales for each nonagricultural pesticide registered. Alternatively, the department could work with the Legislature to revise the statutory requirement to be consistent with the department's practice.

Department Response:

The department agrees with this recommendation and will work with the Legislature to clarify the intent of the \$350 minimum requirement in the statute in question.

Staff Responsible for Implementation: Dan Stoddard

Expected date of completion: May 31, 2016

Finding 2: The Department of Agriculture did not adequately monitor and review timesheet data recorded by employees in the state's payroll system.

Audit Recommendations:

- *The Department of Agriculture should review and document the review of payroll system audit reports in compliance with state policies.*

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- *The Department of Agriculture should review its self service time entry approval assignments and eliminate the ability for employees (as approvers or backup approvers) to approve their own timesheets.*

Department Response:

The department agrees with this recommendation and has taken the following actions.

- Authority for self-approval of timesheets has been removed where it had been mistakenly granted (and never used) and future assignments will be reviewed to ensure this does not happen again.
- Documentation of our review of the self-service time entry report has been improved to add written acknowledgement of review completion on each report and e-mail guidance to employees who completed time entry or approval as a backup if a) notes were not included in the system or b) the action occurred with undue regularity.

We will complete our response with the following action.

- We will implement a system to review the payroll posting audit trail report to verify that employees' time is charged to correct accounts.

Staff Responsible for Implementation: Steve Ernest
Expected date of completion: March 31, 2016

Thank you again for the work that went into this audit. We are committed to taking action to further strengthen our programs and internal controls.

Sincerely,

A handwritten signature in black ink, appearing to read "David J. Frederickson", with a long horizontal flourish extending to the right.

David J. Frederickson
Commissioner