

DEPARTMENT OF AGRICULTURE
FINANCIAL AUDIT
FOR THE FOUR YEARS ENDED JUNE 30, 1990

MAY 1991

Financial Audit Division
Office of the Legislative Auditor
State of Minnesota

DEPARTMENT OF AGRICULTURE

FINANCIAL AUDIT

FOR THE FOUR YEARS ENDED JUNE 30, 1990

Public Release Date: May 30, 1991

No. 91-32

OBJECTIVES:

- **EVALUATE INTERNAL CONTROL STRUCTURE:** payroll, travel, Minnesota Grown Program, Family Farm Security Program, contractual disbursements, and fixed asset inventory control.
- **TEST COMPLIANCE WITH CERTAIN FINANCE-RELATED LEGAL PROVISIONS.**

CONCLUSIONS:

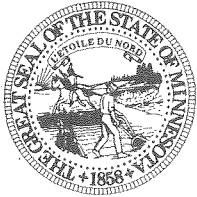
We found the following areas where the internal control structure needed improvement:

- The Family Farm Security Loan Program was not well controlled and required changes in the segregation of duties for the program. We made recommendations in eight aspects of the program and requested the department to be more protective of the state's interest when managing the program.
- The Minnesota Grown Program operated with a nonprofit organization headquartered at the department.
- The department was not adequately safeguarding coupons in the Special Food Program for Women, Infants, and Children.
- Receipt controls over the federal Commodity Credit Corporation warehouse program were inadequate.

We found five areas where the department had not complied with finance-related legal provisions:

- The department needs to develop special assistance farm loan billing procedures to assure that loans are repaid within eight years.
- Guarantees have been improperly extended to refinanced family farm loans as outlined in Minnesota Rules.
- The department has not sold farm properties within three years, as required by statute.
- Minnesota Grown Program staff were depositing advertising and postage fees in a gift fund.
- Commodity Credit Corporation staff, without authority, opened commercial bank accounts to hold seized goods proceeds pursuant to paying claims.

Contact the Financial Audit Division for additional information.
(612) 296-1730



STATE OF MINNESOTA

OFFICE OF THE LEGISLATIVE AUDITOR

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JAMES R. NOBLES, LEGISLATIVE AUDITOR

Representative Ann Rest, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. Elton Redalen, Commissioner
Department of Agriculture

Audit Scope

We have conducted a financial related audit of the Department of Agriculture as of and for the four years ended June 30, 1990. Our audit was limited to only that portion of the State of Minnesota financial activities attributable to the transactions of the Department of Agriculture as discussed in the Introduction. We have also made a study and evaluation of the internal control structure of the Department of Agriculture in effect at June 30, 1990.

We conducted our audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial activities attributable to the transactions of the Department of Agriculture are free of material misstatements.

As part of our examination of the financial statements and our study and evaluation of the internal control structure, we performed tests of the Department of Agriculture's compliance with certain provisions of laws, regulations, contracts, and grants. However, our objective was not to provide an opinion on overall compliance with such provisions.

Management Responsibilities

The management of the Department of Agriculture is responsible for establishing and maintaining an internal control structure. This responsibility includes compliance with applicable laws, regulations, contracts, and grants. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that:

- assets are safeguarded against loss from unauthorized use or disposition;
- transactions are executed in accordance with applicable legal and regulatory provisions, as well as management's authorization; and

- transactions are recorded properly on the statewide accounting system in accordance with Department of Finance policies and procedures.

Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

Internal Control Structure

For purposes of this report, we have classified the significant internal control structure policies and procedures in the following categories:

- payroll,
- travel disbursements,
- Minnesota Grown Program receipts and disbursements,
- Family Farm Security Loan Program transactions,
- contractual disbursements, and
- fixed asset inventory control.

For all of the internal control structure categories listed above, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk.

Conclusions

Our study and evaluation disclosed the conditions discussed in findings 1 to 12 involving the internal control structure of the Department of Agriculture. We consider these conditions to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the entity's ability to record, process, summarize, and report financial data.

A material weakness is a reportable condition in which the design or operation of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We believe the reportable conditions on the Family Farm Security Loan Program described in findings 1-8 represent a material weakness.

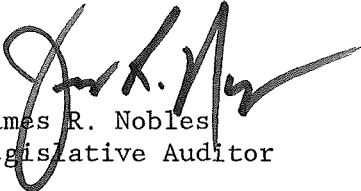
We also noted other matters involving the internal control structure and its operation that we reported to the management of the Department of Agriculture at the exit conference held on April 16, 1991.

Representative Ann Rest, Chair
Members of the Legislative Audit Commission
Mr. Elton Redalen, Commissioner
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The results of our tests indicate that, except for the issues discussed in findings 3, 5, 7, 10, and 12, with respect to the items tested, the Department of Agriculture complied, in all material respects, with the provisions referred to in the audit scope paragraphs. With respect to items not tested, nothing came to our attention that caused us to believe that the Department of Agriculture had not complied, in all material respects, with those provisions.

This report is intended for the information of the Legislative Audit Commission and management of the Department of Agriculture. This restriction is not intended to limit the distribution of this report, which was released as a public document on May 30, 1991.

We would like to thank the Department of Agriculture staff for their cooperation during this audit.



James R. Nobles
Legislative Auditor



John Asmussen, CPA
Deputy Legislative Auditor

END OF FIELDWORK: October 1, 1990

REPORT SIGNED ON: May 23, 1991

DEPARTMENT OF AGRICULTURE

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AUDIT PARTICIPATION

The following members of the Office of the Legislative Auditor prepared this report:

John Asmussen, CPA	Deputy Legislative Auditor
Warren Bartz, CPA	Audit Manager
Jean Mellett, CPA	Auditor-in-Charge
Karen Klein	Auditor
Susan Rumpca	Auditor

EXIT CONFERENCE

The findings and recommendations in this report were discussed with the following staff of the Department of Agriculture at the exit conference held on April 16, 1991:

Elton Redalen	Commissioner
Herbert Halverson	Assistant Commissioner
William Oemichen	Legal Counsel
Joseph Komro	Accounting Manager
Alan Dupay	Assistant Director for Audits
Wayne Marzolf	Director, Family Farm Security Loan Program
Felix McGovern	Director, Grain Licensing and Audit Division
Carol Milligan	Management Analyst
Kevin L. Edberg	Agricultural Marketing Specialist

DEPARTMENT OF AGRICULTURE

I. INTRODUCTION

The Department of Agriculture is primarily a regulatory agency. The department operates under Minn. Stat. Sections 17-34 and 40-42, and administers programs which promote agriculture, the family farm, and conservation practices. It encourages the development of agricultural industries through market development, both nationally and internationally. During the audit period, the department was headed by Jim Nichols, a commissioner appointed by the Governor. Elton Redalen was appointed commissioner in January 1991.

Activities of the Department of Agriculture are financed mainly by appropriations from the General Fund and departmental receipts consisting primarily of license, registration, and service fees. The following financial summary shows department expenditures for fiscal years 1989 and 1990.

	<u>Year Ended June 30</u>	
	<u>1989</u>	<u>1990</u>
Payroll	\$14,526,083	\$16,019,656
Contractual expenses	4,248,396	3,615,194
Miscellaneous operating expenses	1,811,491	1,779,028
Supplies	774,074	845,524
Capital equipment	611,421	1,122,525
Real property	3,298,976	646,783
Grants and aids	2,206,757	2,628,123
Nonexpense disbursements	998,382	1,369,398
Redistributions	<u>128,169</u>	<u>490,824</u>
Total	<u>\$28,603,749</u>	<u>\$28,517,053</u>

Source: *Managers Financial Report* as of September 1, 1990.

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II. CURRENT FINDINGS AND RECOMMENDATIONS

A. Family Farm Security Loan Program

The Family Farm Security Loan Program (FFSP) was established in 1976 to "aid farmers in obtaining credit for the acquisition of real estate." The program offered two forms of assistance: guarantees to lenders and loans to program participants. The loan guarantee provides for the state to pay lenders when participants default on loan payments. The state pays either 90 or 100 percent of the outstanding balance of the loan, depending upon whether the lender has previously reduced the outstanding balance of the loan by a minimum of ten percent. To fund the guarantee obligations, the state established a special bond account for the program. Pursuant to Minn. Stat. Section 41.56, Subd. 4B, proceeds from the sale of farms obtained with bond proceeds shall be returned to the bond fund to the extent that funds were issued.

The program provides for two types of loans:

- Payment adjustment loans provide for the state to annually pay to the lender interest equal to four percent of the loan balance. Participants whose net worth remains under \$135,000 may receive payment adjustment loans for up to twenty years, if participants have complied with other terms of the loan guarantee. Participants must repay payment adjustment loans in either their 11th or 21st year on the program, depending upon whether mandatory extensions have deferred participant repayment to the 21st year.
- Special assistance loans provide that if participants "cannot meet scheduled loan payments because of unique or temporary circumstances," the state may pay participants' loan obligations for up to two consecutive years. Participants must repay special assistance loans, with interest, within eight years.

The program is not well controlled and requires changes in the control environment. The department must be more protective of the state's interest when managing the program. The following eight findings illustrate this conclusion.

1. Duties over the Family Farm Security Program are improperly segregated.

FFSP administrative and recordkeeping duties are mainly in the Family Farm Security Program section and are inadequately separated. FFSP staff both administer the FFSP program (including payment adjustment and special assistance loans, guarantees, and tax refunds) and maintain program records. Program staff are responsible for both loan payments and repayments. FFSP staff authorize loan payments, bill and collect loan

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repayments, and maintain loan receivable records. Program staff negotiate leases and rents for acquired property, collect rent receipts, and attend mediations where they make binding agreements on behalf of the state. FFSP staff are responsible for administering the agreements, as well as maintaining records documenting the agreements. Program staff authorize the payment of guarantees, manage and sell acquired property, and maintain property income and expense records.

Administrative and recordkeeping duties are incompatible. Many problems are caused by concentrating duties in the FFSP section. The duties seem to be too many for a limited staff to control. Staff who are responsible for both program and recordkeeping duties may not detect errors or irregularities. We believe that some problems would be resolved if the program authority, access to assets, or record keeping were shifted to somewhere else in the department. Findings two through eight discuss examples of incomplete records, inconsistent calculations, and untimely transactions. An adequate separation of duties is necessary to ensure that transactions are properly recorded, properly documented, properly valued and reasonable.

Currently, the department's Accounting Division performs limited duties in the FFSP section. To ensure an adequate separation of duties, the Department of Agriculture's Accounting Division needs to maintain Family Farm Security Loan Program records, including subsidiary rent receivable records. The Accounting Division also should calculate loan interest, bill receivables, and collect receivables. Segregation of duties would help lack of timeliness, poor documentation, inconsistent calculations, and completeness.

RECOMMENDATION

- The department's Accounting Division should become more involved in the Family Farm Security Program by:
 - maintaining program records, and
 - billing and collecting receivables.

2. The department needs stricter accounting controls over payment adjustments.

Controls over payment adjustments are not sufficient to ensure that accounts receivable due from former program participants are recorded. One participant assumed his loan from a former participant in 1986. The former participant did not repay his \$26,700 payment adjustment loan. Rather, he signed a Consent to Assignment and Assumption Agreement which stated that the purchase was "subject to the State releasing its current lien on the property." Despite the assumption agreement, FFSP staff did not request the Executive Council to forgive the amount owed by the former participant. Although the debt has not been resolved, the former participant's payment adjustment liability does not appear on the FFSP participant report.

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The FFSP participant report is a financial summary report identifying the status of past and present participants. The summary includes defaults and withdrawals, interest adjustment paid, interest reimbursed and forgiveness/loss. However, the report does not include participants who left the program before the FFSP began a comprehensive computer list of participants. The department needs to account for participants excluded from the report to determine whether participants have outstanding loans with the state. Financial summary information must include the disposition of all program loans.

Controls are not sufficient to ensure that scheduled payment adjustments are correct in amount. Specifically, controls to determine whether participants have made special principal payments are inadequate. Two sample participants made additional payments to lenders for several years before FFSP staff became aware of the payments. One participant made special principal payments totaling \$8,012 over a three year period. Neither the participant nor the lender informed FFSP staff of the special principal payments. Consequently, FFSP overpaid the participant's payment adjustments by approximately \$176. FFSP staff did not require the lender to repay the state the additional interest paid, but adjusted the participant's schedule balance. After staff adjusted the payment schedule, the participant made additional special principal payments of \$3,498 without informing FFSP staff. Correct schedule balances are important because payment adjustments are equal to four percent of the outstanding principal balance of the Family Farm loan. The state overpays interest when the participant's schedule is not adjusted for special principal payments.

The department needs to develop controls to ensure that participants' schedule balances are correct. FFSP staff annually receive certified statements from lenders and participants. Lenders sign a Request for Payment, certifying that loan principal balances are correct. Participants submit current net worth statements. Net worth statements include real estate mortgage information. FFSP staff often adjust participants' net worth statements, including information regarding real estate mortgages and the number of acres of land the participant owns, because the information does not agree with FFSP records. Staff must not correct participant reported information without thoroughly investigating the reason for the discrepancy. FFSP staff need to emphasize the importance of accurate reporting to participants and lenders.

RECOMMENDATIONS

- The department should include all participants who closed on the program on the FFSP participant report.
- The department should develop controls to ensure that participants' schedule balances are correct. FFSP staff should request repayment of excess interest paid to banks.
- The department should not change participant reported net worth information without thoroughly documenting the reason.

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3. The Department of Agriculture needs to develop special assistance billing procedures.

Family Farm Security Program (FFSP) special assistance billing procedures are inconsistent. FFSP staff do not use a uniform method to compute interest, have not set policy for accruing late interest, and have not developed a policy to ensure that loans are repaid within eight years as required by Minn. Stat. Section 41.56, Subd. 3.

FFSP staff use two different methods to calculate special assistance interest for participants who owe past due principal and interest. The difference in the two methods is the rate used to calculate interest on past due principal balances. As required by Minn. Stat. Section 41.56, Subd. 3, participants pay interest "at an annual percentage rate four percent below the prevailing Federal Land Bank rate." Staff sometimes apply the current Federal Land Bank rate to total unpaid principal balances. However, staff sometimes calculate interest in steps, using prior years' Federal Land Bank rates on past due principal and the current rate on the remaining balance. Staff need to calculate interest using a uniform rate.

FFSP staff do not have a policy for accruing interest on payments which are late but paid in the year that they are due. Generally, FFSP staff do not assess accrued interest on late principal payments. In one case, a participant did not pay accrued interest on a payment made three months late. However, FFSP sent a letter to another participant advising him that interest would accrue on any principal portion of a payment over six months delinquent. FFSP staff need to assess accrued interest whenever a payment is past due.

FFSP staff have not developed an effective collection policy. Currently, 21 participants have special assistance loans outstanding. As of June 30, 1990, only eight participants had made all scheduled payments. FFSP staff send billings approximately three weeks before payments are due. FFSP staff also send billing follow-up letters every two months. FFSP staff have not used revenue recapture or attorney general's letters to collect payments.

RECOMMENDATIONS

- The department should use a uniform interest calculation.
- The department should assess interest on late payments.
- The department should develop an effective collection policy for FFSP loans.

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4. Participants have sold portions of land covered by the FFSP guarantee.

The department needs to be sure that guarantee participants do not sell portions of their land. Specifically, staff need to determine if participants who sell land are eligible to receive the full four percent payment adjustment and whether the participant should reimburse the state for past payment adjustments.

Some participants have sold portions of land covered by the FFSP guarantee. One participant sold 88 of 240 acres of guaranteed land. The participant did not make a special principal payment. FFSP staff continued to make the full four percent payment adjustments based on the participant's loan schedule. The participant subsequently defaulted. In mediation, the state agreed to forgive the participant's payment adjustment loan and his two special assistance loans in exchange for assignments of contracts for deed on the land he sold. The contracts totalled approximately \$33,863 less than the loan amounts. The holder of two contracts has not made any payments to the state, and the state has filed a complaint against him.

Controls over sales for portions of land covered by the state guarantee are inadequate to protect the state from loss. Minn. Stat. Section 41.59 states:

Any participant who sells or conveys the property for which a family farm security loan was issued shall immediately retire the entire indebtedness still owed to the lender and the commissioner.

The FFSP director believes that Minn. Stat. Section 41.59 pertains only to sales of the total acreage under the guarantee. The director stated that he considers the following when a participant decides to sell land:

- The importance of the land parcel to the farming operation.
- Whether the participant continues to farm.
- Whether the sale is part of a financial arrangement.
- Whether the participant plans to make a special principal payment.

The department needs to develop policies to protect the state from loss. FFSP staff need to determine whether the FFSP program should continue to make full four percent payment adjustments if the participant does not make a special principal payment. Staff also need to consider whether the participant ought to repay part of the payment adjustment loan.

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RECOMMENDATION

- The department should protect the state's interest when participants sell land covered by the guarantee. The department should not allow participants to sell off parts of guaranteed land.

5. Guarantees have been improperly extended to refinanced loans.

FFSP staff have extended loan guarantees to new lenders. Loan term extensions do not comply with Minn. Rules 1560.2300, Subpart 2.D. We noted two cases where participants were allowed to refinance new loans and extend the state's guarantee.

Minn. Rules 1560.2300, Subpart 2.D. provides for guarantee extensions as follows:

An extension must be granted to the length of a loan that would require a balloon payment in ten years or less and the stated interest rate may be adjusted by consent of all parties to the loan including the state, the participant, and the lender, if the following conditions are met:

- (1) the participant and lender both sign a written request for extension;

Five of 24 sample participants received loan term extensions. Two of the five sample participants who received guarantee extensions entered into new refinancing arrangements after their original contracts expired.

- One sample participant's contract for deed expired on April 1, 1989. The participant refinanced with a new lender bank on June 6, 1989, and the new lender did not request the guarantee in writing. FFSP files contain no information to show that the loan was contingent on the guarantee.
- In another case, the participant and the new lender also did not sign a written request for extension. The lender did not indicate that the loan was contingent on the state's guarantee. The state also subordinated its \$19,652 payment adjustment lien when the participant refinanced, even though FFSP files do not show that the bank requested a subordination. A letter from FFSP staff to the bank stated "I'm assuming your attorney will say you need a subordination of our lien to get your mortgage into first position. Enclosed is that subordination."

We do not think the two cases are covered under the rule or that the new arrangements are in the best interests of the state.

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RECOMMENDATION

- FFSP staff should not extend guarantees to refinanced loans.

6. Mediated agreements lack documentation.

Some state agreements made pursuant to the Farmer-Lender Mediation Act of 1986 are not supported by a mediation "Memorandum of Agreement". Signed Memorandums of Agreement are necessary because the Farmer-Lender Mediation Act of 1986 provides authority for FFSP agreements which are not authorized by Minn. Stat. Chapter 41. The state, through its Executive Council designee, approves debt compromises arising from mediation. Memorandums of Agreement should support all debt compromises arising from mediation. Mediation agreements sometimes do not support state settlements.

- One mediation closed with a "Mediation Conclusion With No Agreement" which all parties, including the state and the participant, signed. Shortly thereafter, the state and the participant executed an agreement which states:

The execution of this agreement is in partial fulfillment of those conditions agreed to during the mediation process.

FFSP staff explained that the participant and the state had discussed the terms of the agreement during mediation. However, the agreement was reached after mediation closed.

- Some state agreements included terms which are not included in mediation memorandums of agreement. For example, one mediation closed with an agreement that the sellers "exercise their State of Minnesota guarantee." The subsequent agreement between the state and the participant provided for the state to sell back the property to the participant.
- In some cases, FFSP files did not include a mediation conclusion document. One seller whose guarantee was bought out by the state complained to the Attorney General's Consumer Services Division that "The new contract says we've had mediation. We did not have mediation" (seller's emphasis). In this case, FFSP files include a summary of one mediation session, but the files do not include a mediation Memorandum of Agreement.

The department needs to document the results of mediations with Memorandums of Agreement, which document staff authority to make agreements not authorized by Minn. Stat. Chapter 41. The existence of signed memorandums of agreement may also prevent potential lawsuits.

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RECOMMENDATION

- The department needs to support mediated agreements with signed Memorandums of Agreement.

7. The department has not properly managed property.

The department has allowed participants to live on property rent free for up to two years. FFSP staff sometimes have not cancelled contracts for deed promptly.

- In one case, FFSP paid out on a guarantee in October 1985, but FFSP staff did not cancel the participant's contract until June 30, 1989. Although this case was complicated by a bankruptcy, files indicate the bankruptcy closed two years prior to the contract cancellation. Consequently, the farmer lived on the land rent free for two years.
- In another case, the state paid out the guarantee and received assignment of the contract in December 1987. The state did not cancel the contract until June 1989. Between the time of payout and contract cancellations, participants lived on the land rent free. The state cannot rent or sell the property until the state cancels the contract.

The department has not sold farm properties within three years, as required by statute. FFSP staff currently rent 22 properties, approximately 17 of which were acquired between 1985 and 1987. Minn. Stat. Section 41.56, Subd. 4 requires staff to sell property "within three years after the conveyance of title to the state or after the expiration of the period of redemption".

RECOMMENDATION

- The department should cancel contracts for deed promptly, so that the state can rent or sell land.
- The department should sell properties within three years after conveyance of title to the state.

8. Farm sale documentation is incomplete.

FFSP staff do not consistently document farm values, do not record bids for property if the offer is not accepted, and do not retain copies of farm sale advertisements.

FFSP staff do not consistently document farm values. Only three of six files tested included some type of farm value summary. Also, files do not include information explaining reasons farms sell below their apparent

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value. In September 1989, staff sold one property through a Realtor for \$32,000. The 1989 and 1990 estimated market value of the property was \$94,600 and \$82,900, respectively. The sale was the second time FFSP sold the property to the same person. Staff first sold the property in 1985 for \$55,000. The buyer defaulted in late 1988 after paying \$2,000 principal and \$2,500 interest. FFSP files do not contain either an appraisal or a Realtors' sales analysis of the property. Files also do not show that FFSP staff advertised the farm, because no advertising invoices or ad copies were in the file. The files also do not show if there were any other offers for the property. FFSP staff stated that there were no other offers for the farm, that the selling price was low because the property sold for cash, and that the property was overvalued when it was accepted on the program.

As discussed in our prior audit report, FFSP staff need to obtain appraisals to ensure that the terms of farm sales are in the state's best interests. FFSP staff also need to retain copies of farm ads to verify that they placed advertising in compliance with Minn. Stat. Section 41.56, Subd. 4.

RECOMMENDATION

- The department should document farm values with appraisals, document all bids for properties, and retain copies of farm sale advertisements.

B. Operating Receipts and Disbursements

9. The Minnesota Grown Program allows a nonprofit organization headquartered at the Department of Agriculture.

Headquartering of the nonprofit corporation, Minnesota Grown Promotion Group, at the Department of Agriculture (DOA) creates problems for both DOA and the corporation. The similarity of the state program to the nonprofit corporation confuses the public. The DOA Minnesota Grown Programs uses similar names and advertising.

The presence of the Minnesota Grown Promotion Group has adversely affected receipt controls. Because of the similarity of the nonprofit corporation name to the state program name, the mailroom has difficulty determining whether mail is for Minnesota Grown Promotion Group or DOA Minnesota Grown Program. Therefore, mailroom staff send receipts directly to program staff without restrictively endorsing checks. Minnesota Grown Program staff also are confused by the similarity in names. Minnesota Grown staff do not know if checks made payable to Minnesota Grown are meant for the department program or the nonprofit corporation. On one occasion, DOA program staff deposited a Minnesota Grown Promotion Group check in the state depository. Confusion of the nonprofit corporation name with the program name also may cause the public to give money to the wrong organization.

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We are concerned that the department has not delineated clear lines of authority between itself and the nonprofit corporation. The nonprofit corporation does not function as an autonomous entity and often is confused with the state program. Department employees perform functions for both the state and the nonprofit corporation. The administrator of the state Minnesota Grown program, who also is the chairperson of the nonprofit Minnesota Grown Promotion Group, holds advisory committee and board meetings together. State program advisory committee members are also members of the nonprofit corporation board. State employees are members of the Minnesota Grown nonprofit corporation and attend Minnesota Grown Promotion Group meetings on state time. Minnesota Grown, DOA, and Minnesota Grown Promotion Group minutes are not separate from one another. State employees write up board minutes on state time.

We believe that the department must reconsider the need for its relationship with the nonprofit corporation. However, if the department elects to maintain its relationship with the nonprofit corporation, the department must:

- enter into a formal agreement with the nonprofit corporation disclosing each party's rights and responsibilities;
- inform the public that the state program is separate from the Minnesota Grown Promotion Group; and
- properly record all receipts and disbursements.

We believe the problems are best remedied by severing the relationship to the nonprofit corporation.

RECOMMENDATIONS

- DOA should resolve the problems presented by its relationship with the nonprofit corporation.
- Minnesota Grown Program staff should require donors to make checks payable to the Department of Agriculture.

10. Minnesota Grown program staff are depositing advertising and postage fees in a gift fund.

Minnesota Grown staff improperly deposit advertising and postage fees into a gift account. During fiscal year 1990, directory listing fees totalled \$2,008 and postage fees totalled \$49. The department suggests a contribution for these costs.

DOA distributes a directory of Minnesota's roadside stands, orchards, pick-your-own farms, and farmer's markets. To advertise in the directory, organizations usually submit \$10 to the Minnesota Grown matching account. If organizations want to display directories at their location, they usually pay a \$2 postage charge. The Minnesota Grown program does not have the authority to generate matching funds with these fees. Minn. Stat. Section 16A.72 states that "all income, including fees or receipts of any nature, shall be credited to the General Fund."

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RECOMMENDATION

- DOA should not deposit advertising and postage fees in the gift account.

11. DOA is not adequately safeguarding WIC coupons.

Controls over coupons in the Special Food Program for Women, Infants, and Children (CFDA #10.557) are inadequate. Specifically, staff do not adequately safeguard and cancel used coupons.

The WIC program issues coupons to disadvantaged women with infants and children to purchase Minnesota Grown fruits and vegetables at farmer's markets. Farmers submit coupons to DOA for reimbursement. The WIC administrator keeps WIC coupons in an open area until she counts them. After she counts the coupons, she sends them to the Accounting Division. The Accounting Division keeps the coupons under a desk until they expire. Unexpired coupons are reusable unless they are voided. Staff need to cancel coupons to prevent them from being stolen and reused.

RECOMMENDATION

- DOA staff should void or secure WIC coupons at the time of receipt.

12. Receipt controls over the federal CCC (Commodity Credit Corporation) warehouse program are inadequate.

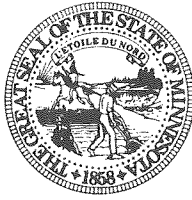
Controls over the federal cooperative warehouse program are not adequate to ensure that funds are deposited in the proper account. Specifically, CCC warehouse staff have deposited federal receipts in the division's Special Revenue Fund account. Staff coded two of three special examination deposits to the Special Revenue Fund, rather than the Federal Fund. Staff said that they were not aware of deposit miscodings because they do not receive statewide accounting receipts reports from the central office in St. Paul. Central office staff currently reconcile CCC warehouse receipts for the division. Central office staff, however, do not receive sufficient documentation to detect receipts coding errors. Central office staff should send copies of receipts reports to CCC warehouse staff. An independent CCC Warehouse staffperson should reconcile receipts. Staff should correct miscoded deposits.

Periodically, CCC warehouse staff open a commercial bank account to hold seized goods proceeds pursuant to paying claims. The department does not have the authority to maintain an account outside the state system. Staff stated that they maintain funds in a commercial bank account because Minnesota Rule 1562.2000 requires the proceeds to draw interest. Currently, state accounts draw interest only if interest is authorized by statute. A conflict exists between statute and rule. The department needs to seek statutory authority to receive interest on seized goods accounts.

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RECOMMENDATIONS

- DOA should correct miscoded deposits.
- DOA should reconcile receipts to statewide accounting receipts reports monthly.
- DOA should deposit seized goods money in a state account.



LAND OF QUALITY FOODS
OFFICE OF THE COMMISSIONER

90 W. PLATO BOULEVARD
SAINT PAUL, MN 55107

STATE OF MINNESOTA
DEPARTMENT OF AGRICULTURE

May 17, 1991

Mr. James R. Nobles, Legislative Auditor
Office of the Legislative Auditor
Veteran's Service Building
Saint Paul, Minnesota 55155

Dear Mr. Nobles:

This is my first opportunity to participate in the findings of a legislative audit which covers the four year period which ended June 30, 1990. I want to assure you that even though the audit period covers a time frame prior to my becoming Commissioner, we take this process seriously and will fully cooperate and implement the recommendations provided by your staff.

The Family Farm Security Loan Program (FFSP) is a special state program established to assist beginning farmers to purchase farm real estate. The first applicants were approved into the program in March, 1977. No new applications have been approved since January, 1986. The first special assistance loan was approved in June, 1985, and no new special assistance loans have been granted since March, 1987. The department has been selling acquired properties since 1981. The first default occurred in June, 1980.

There has been an audit of the FFSP each year since at least 1980. Program administration, recordkeeping duties and procedures have changed little over the past ten years, except in response to given audit recommendations.

We have reviewed your recommendations and provide the following responses concerning your audit of the Department of Agriculture for the four years ended June 30, 1990.

1. Duties over the Family Farm Security Program are improperly segregated.

RECOMMENDATION

- The department's Accounting Division should become more involved in the Family Farm Security Program by:
 - maintaining program records, and
 - billing and collecting receivables.

DEPARTMENT RESPONSE: The agency agrees with this recommendation. Further, I have directed that Mr. Wayne Marzolf, the Manager of the Family Farm Security Program and Mr. Joseph Komro, Accounting Division Manager develop special procedures for billings and receipt collection as well as maintaining program records by July 1, 1991.

2. The department needs stricter accounting controls over payment adjustments.

RECOMMENDATIONS

- The department should include all participants who closed on the program on the FFSP participant report.



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DEPARTMENT RESPONSE: The Records Retention Schedule approved in 1981 for the Family Farm Security Program provides that one year after the participant has reimbursed the state for any interest adjustment payments made on his/her behalf, the file may be disposed of. The files for those participants who withdrew through 1984 and reimbursed the state were destroyed in accordance with this schedule. I have directed that no additional files be disposed of, and that every effort be made to reconstruct this information. This information will be included in the Family Farm Security Program participant report effective immediately and has been assigned to Wayne Marzolf.

- The department should develop controls to ensure that participant's schedule balances are correct. Family Farm Security Program staff should request repayment of excess interest paid to banks.

DEPARTMENT RESPONSE: Annually, a Request For Payment Adjustment form is sent to all cooperating lenders that will be receiving a payment adjustment in a given loan year. This form serves as an invoice and states the current principal balance that our records indicate. The lender signs a statement that says, in part: "I hereby certify the principal balance is correct as shown above" We also receive annually a current Net Worth Statement from each participant. The participant signs this form, which contains a statement that the information given is: ". . . a true, complete, and accurate statement of my financial condition . . ." If the information on the two reference forms conforms with our records, it was assumed that the schedule balances are correct. I have directed that the Family Farm Security Staff immediately notify by letter to all lenders and participants emphasizing the importance of providing timely notice of any special principal payments made by participants.

Also, the agency will recover any excess interest paid. Beginning immediately, staff will demand repayment of excess interest paid, and until settled, no further interest payments will be paid on a loan.

- The department should not change participant reported net worth information without thoroughly documenting the reason.

DEPARTMENT RESPONSE: Effective immediately, Family Farm Security Program staff will require written explanations for discrepancies from either the participant or the Family Farm Security Program reviewer. Any changes will be fully documented in writing. A specific set of instructions has been provided each participant to guide them in properly completing the Net Worth Statement. Prior to authorization of interest adjustment payments, the Net Worth Statement is carefully reviewed by Family Farm Security Program staff. Any errors in mathematics and deviations from the instructions are noted and corrected to maintain a consistency in net worth determination. A trend sheet is kept in the net worth section of each participant's file. Staff corrections are noted on that trend sheet for anyone to review. Any significant changes are communicated in writing (a carbon copy of all letters can be found in the correspondence section of each file) to the participant.

3. The Department of Agriculture needs to develop special assistance billing procedures.

RECOMMENDATIONS

- The department should use a uniform interest calculation.

DEPARTMENT RESPONSE: The agency has already implemented this recommendation and now uses one method of interest calculation and has assigned this recommendation to Mr. Wayne Marzolf.

- The department should assess interest on late payments.

DEPARTMENT RESPONSE: The agency will implement this recommendation immediately by calculating any additional interest, to the extent allowed by law, based upon the date of receipt of payment. Implementation of this recommendation was assigned to Wayne Marzolf of the Family Farm Security Program.

- The department should develop an effective collection policy for Family Farm Security Program loans.

DEPARTMENT RESPONSE: The Department will implement collection procedures for all outstanding special assistance payments, etc. by July 1, 1991. Mr. Joseph Komro, Accounting Division Manager and Mr. Wayne Marzolf, Family Farm Security Program Manager will develop written procedures to fully coordinate the collection of all scheduled payments and billings to include using existing Accounting Division collection procedures.

4. Participants have sold portions of land covered by the FFSP guarantee.

RECOMMENDATION

- The department should protect the state's interest when participants sell land covered by the guarantee. The department should not allow participants to sell off parts of guaranteed land.

DEPARTMENT RESPONSE: The agency agrees that it will not allow Family Farm Security Program participants to sell portions of land covered by the Family Farm Security Program guarantee.

In the rare case where the Department determines such a sale will demonstrably protect the state's interest, the agency agrees there needs to be a definitive, written policy concerning the sale of portions of land covered by the Family Farm Security Program guarantee. The agency will develop a policy for implementation by July 1, 1991. Further, the agency will make this policy available to your staff for review before July 1, 1991. It will include a review process whereby the advice and recommendation of the Family Farm Advisory Council will be obtained in cases where more than a nominal acreage or value is involved. The review will also examine the possibility of the participant's withdrawal from the program as a condition for state approval of the transactions.

The new policy will require the continued review of the request by the Attorney General's Office. The Attorney General's Office has agreed to place its file evaluations and recommendations in writing.

5. Guarantees have been improperly extended to refinanced loans.

RECOMMENDATION

- FFSP staff should not extend guarantees to refinanced loans.

DEPARTMENT RESPONSE: The agency agrees that it will not extend guarantees to refinanced loans except where the extension will demonstrably protect the state's financial interest. In certain cases, the alternative to extension of the guarantee and the underlying loan would be default by the participant and a guarantee payout that would exceed the land's value. Default is the most detrimental situation for the state and produces certain losses.

The agency will better document Family Farm Security Program guarantee extensions to demonstrate that funding was not available without the state's guarantee and will be reviewed with the Family Farm Advisory Council for their advice and recommendation prior to the grant of any extension. In the rare case where an extension is warranted, the processing will be completed prior to the expiration date of the original loan.

6. Mediated agreements lack documentation.

RECOMMENDATION

- The department needs to support mediated agreements with signed Memorandums of Agreement.

DEPARTMENT RESPONSE: The agency concurs with this recommendation. In mediation, Mr. Wayne Marzolf, Family Farm Security Program Manager, has been directed to require the

mediator to provide a signed mediation-ending document in all future mediation cases involving the Family Farm Security Program.

7. The department has not properly managed property.

RECOMMENDATIONS

- The department should cancel contracts for deed promptly, so that the state can rent or sell land.

DEPARTMENT RESPONSE: The agency has already implemented this recommendation. I have directed that the Family Farm Security Program staff vigorously pursue a schedule of direct contacts with all responsible parties in a given case so that title is cleared on a timely basis. Mr. Marzolf has been directed to have in place written procedures regarding the above by July 1, 1991.

- The department should sell properties within three years after conveyance of title to the state.

DEPARTMENT RESPONSE: The agency agrees with this recommendation and the Family Farm Security Program Staff will continue to vigorously pursue the sale of acquired properties until the inventory is completely liquidated.

8. Farm sale documentation is incomplete.

RECOMMENDATION

- The department should document farm values with appraisals, document all bids for properties, and retain copies of farm sale advertisements.

DEPARTMENT RESPONSE: I have directed Family Farm Security Program staff to more fully document the file concerning their contacts and information received. A written market analysis on the property will be solicited from the listing agent prior to beginning the sale process and a final written report will be required from the listing agent.

The agency advertises four consecutive weeks in the primary local newspaper in the area of the subject farm. Additional advertising is placed in area weeklies, regional shoppers and major papers outside the immediate area, depending on the size, type and desirability of the property. No advertising invoices are paid until a tear sheet from the publisher is received. Once the farm sale has been closed, all expenses paid and administrative actions completed, extraneous materials, including the tear sheets, are cleaned out of the file to reduce the bulk storage needed. Family Farm Security staff will retain tear sheets on all sales.

9. The Minnesota Grown Program allows a nonprofit organization headquartered at the Department of Agriculture.

RECOMMENDATIONS

- DOA should resolve the problems presented by its relationship with the nonprofit corporation.

DEPARTMENT RESPONSE: The Marketing and Promotion activity of the department will resolve any problems or confusion presented by its close working relationship with the promotional nonprofit corporation. All communications and printed material will specify the Minnesota Grown Program of the Department of Agriculture when it is a department document or function. Further, the department will not allow any state employee of this agency to serve as a board member of the Minnesota Promotion Group.

The department will also enter into a formal agreement with the nonprofit corporation outlining each party's rights, duties, cooperation and responsibilities so that the public and state program are maintained separately from the nonprofit program. As part of this agreement, the department will also ask for appropriate financial statements even though the agency does not

provide the Minnesota Grown Promotion Group with funds, but cooperates with it to promote Minnesota Grown agricultural products as authorized by Minnesota Statutes Sections 17.03, 17.101, and 17.102. This recommendation has been assigned to Mr. Ralph Groschen, Director of the Marketing Division, and will be implemented by October 1, 1991.

- Minnesota Grown Program Staff should require donors to make checks payable to the Department of Agriculture.

DEPARTMENT RESPONSE: The Marketing and Promotion activity of the Department has already implemented this recommendation and will only accept checks payable to the Department of Agriculture, for the specific purpose of being deposited into the Minnesota Grown State Matching Account. This recommendation has also been assigned to Mr. Groschen.

10. Minnesota Grown Program staff are depositing advertising and postage fees in a gift fund.

RECOMMENDATION

- DOA should not deposit advertising and postage fees in the gift account.

DEPARTMENT RESPONSE: The Marketing and Promotion activity has already implemented this recommendation and will no longer deposit directory listing and postage donations into the Minnesota Grown Matching Account. This recommendation has also been assigned to Mr. Groschen.

11. DOA is not adequately safeguarding WIC coupons.

RECOMMENDATION

- DOA staff should void or secure WIC coupons at the time of receipt.

DEPARTMENT RESPONSE: Agency staff has already implemented this recommendation and will void or secure WIC coupons at the time of receipt and until such time as they are no longer needed and are destroyed. This recommendation was assigned to Mr. Komro of the Accounting Division and Ms. Milligan of the WIC Program.

12. Receipt controls over the federal CCC (Commodity Credit Corporation) warehouse program are inadequate.

RECOMMENDATIONS

- DOA should correct miscoded deposits.

DEPARTMENT RESPONSE: Any miscoded deposits for fiscal year 1991 will be corrected or funds transferred as required for prior fiscal years. This recommendation has been assigned to Mr. Felix McGovern, the Director of the Warehouse Program.

- DOA should reconcile receipts to statewide accounting receipts reports monthly.

DEPARTMENT RESPONSE: The Accounting Division will forward each month to all divisions the Statewide Accounting Report for all deposits by appropriation number which were made for each account. Divisions would report any discrepancies upon receipt of the report. The Department does reconcile accounting receipt reports monthly, and the Grain Licensing and Auditing Division will submit copies of all billings under the federal cooperative agreement to the Accounting Division for inclusion in the agency's accounts receivable and federal fund files. This recommendation will be implemented by June 1, 1991, and has been assigned to Mr. McGovern and Mr. Komro.

- DOA should deposit seized goods money in a state account.

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DEPARTMENT RESPONSE: The department concurs in this recommendation and will only deposit seized goods money into an agency fund (fund 61) in the Statewide Accounting System. This recommendation has been assigned to Mr. McGovern.

We appreciate the opportunity to respond to these recommendations and for the cooperation of the staff of your office and this agency during this audit.

Sincerely,

A handwritten signature in cursive script, reading "Elton R. Redalen".

Elton R. Redalen
Commissioner