



PERFORMANCE AUDIT REPORT

Grain Inspection Department

**A Report to the Legislative Post Audit Committee
By the Legislative Division of Post Audit
State of Kansas
August 1985**

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Grain Inspection Department

OBTAINING AUDIT INFORMATION

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GRAIN INSPECTION DEPARTMENT

Summary of Legislative Post Audit's Findings

The Kansas Grain Inspection Department is responsible for determining and certifying the quality of grain produced in the State. It also regulates all public grain warehouses operating under the Public Warehouse Laws. After two grain elevators failed in 1982, the Legislative Division of Post Audit was directed to conduct a performance audit of the Department's Warehouse Division. Because warehouses have continued to fail since 1982, Legislative Post Audit was directed to conduct this follow-up performance audit of the Grain Inspection Department. The audit examined the steps the Department has taken to implement the recommendations of the 1982 audit, as well as the Department's use of State property and resources.

What steps has the Grain Inspection Department taken to implement the recommendations of the 1982 performance audit? The 1982 performance audit made numerous recommendations for improving the Department's operations. These recommendations addressed problems in four areas: licensing procedures, financial protection for grain producers, examination procedures, and enforcement of State laws. A number of the recommendations made required changes in State law or regulation. Others required action only by the Grain Inspection Department. The auditors found that many of the 1982 recommendations requiring changes in law or regulation have been implemented. However, the Grain Inspection Department is not always in full compliance with those new laws. The auditors also found that the Department has implemented some of the recommendations directed toward it, although other recommendations have not been implemented or have been only partially implemented. In two cases, the Department disagrees with the recommendations made in the prior report, and no action has been taken. The auditors concluded that additional improvements are needed in the areas of licensing warehouses and enforcing the Public Warehouse Laws.

Is the Department, in carrying out its mandated activities, complying with all applicable laws and regulations governing the use of State property and resources? The auditors reviewed the Department's policies and procedures for personnel transactions, travel and subsistence expenditures, telephone usage and leasing office space. They found that the Department is generally in compliance with the laws and regulations governing the use of State property and resources. However, the Department could enhance personnel procedures by improving documentation and changing the exit interview process. The auditors also found that five of 32 vehicles permanently assigned to the Grain Inspection Department are not meeting their minimum mileage requirements. With an official policy on phone usage implemented on July 18, 1985, the Department's procedures for monitoring telephone usage appear to be adequate. Finally, the cost of the Department's central office space is only slightly higher than the cost of comparable space for other State agencies.

In accordance with Legislative Post Audit's normal procedures, a draft audit report was sent to the Grain Inspection Department. The Department's written comments are included in Appendix C to this report. Along with those comments the Department supplied documentation that some position vacancies had been posted within the agency and most of the required exit interviews were conducted. The appropriate changes have been made to the text of the final report. The supplemental documentation provided by the Department is available for review at the Legislative Division of Post Audit's offices.

GRAIN INSPECTION DEPARTMENT

The Kansas Grain Inspection Department is responsible for determining and certifying the quality of grain produced in the State. It also regulates all public grain warehouses operating under the Kansas Public Warehouse Laws. After two grain warehouses failed in 1982, the Legislative Division of Post Audit was directed to conduct a performance audit of the Department's Warehouse Division. That report, issued in December 1982, made numerous recommendations for improving the laws and procedures for licensing and examining public warehouses, enforcing the Public Warehouse Laws, and providing financial protection for grain producers.

The 1983 Legislature enacted a number of laws designed to strengthen the Kansas Public Warehouse Laws. Additional changes were made in 1984 and 1985. Despite these changes, grain warehouses continue to fail. While 11 State-licensed warehouses failed during the 20-year period from 1963 to 1982, eight more warehouses failed just between January 1983 and June 1985.

At its meeting on May 15, 1985, the Legislative Post Audit Committee directed the Legislative Division of Post Audit to conduct a follow-up performance audit of the Grain Inspection Department. Specifically, this audit addresses the following questions:

1. What steps has the Grain Inspection Department taken to implement the recommendations of the 1982 performance audit?
2. Is the Department, in carrying out its mandated activities, complying with all applicable laws and regulations governing the use of State property and resources?

A Brief Description of the Grain Inspection Department

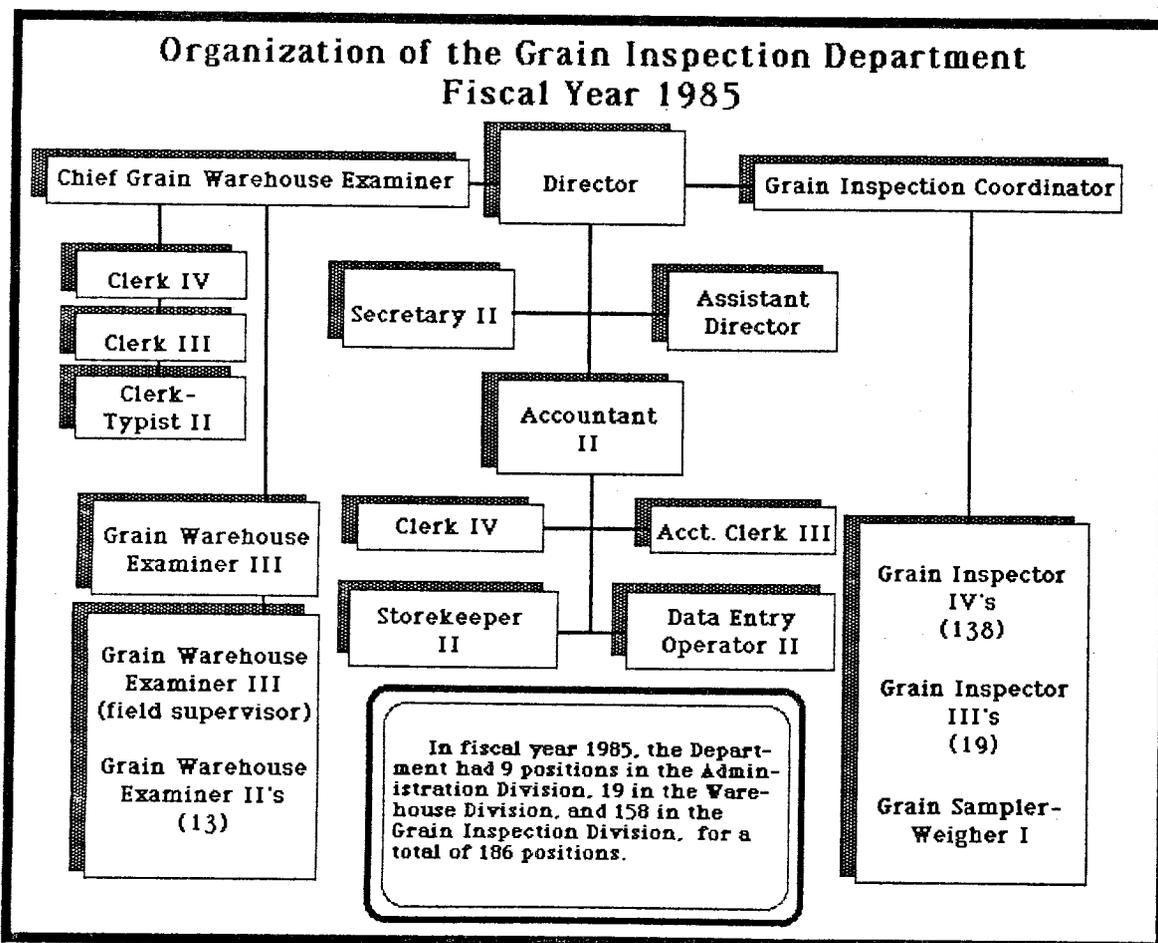
The Grain Inspection Department was established by the Legislature in 1897, at the request of the grain industry. Initially, the Department was responsible only for sampling grain and certifying its official weight and grade. In 1907, the Legislature enacted the Public Warehouse Laws and assigned the duty of enforcing them to the Grain Inspection Department.

The Department is managed by a Director who is appointed by, and serves at the pleasure of, the governor. The Director receives advice and counsel from the Grain Advisory Commission. Established by the Legislature in 1953, the Commission is composed of five members appointed by the governor. These five members serve staggered three-year terms and include a banker, a farmer, a representative of a cooperative, a terminal elevator representative, and a country elevator representative.

The Department is organized into three divisions: the Administrative Division, the Inspection Division, and the Warehouse Division. The Administra-

tive Division is responsible for recordkeeping, accounting, and other centralized functions. The Inspection Division, which has field offices in eight locations across the State, samples, weighs, inspects, and certifies the official grade of grain. The Warehouse Division administers the Public Warehouse Laws. The warehouse examiners inspect all State-licensed warehouses and work out of their homes in cities across Kansas.

The Department was authorized to have 186 permanent employees during fiscal year 1985, as well as a varying number of temporary and emergency employees. These temporary and emergency appointments are generally made during and following the harvest season to assist in the sampling and testing of grain. The organizational chart below shows the distribution of the Department's positions.



The Grain Inspection Department is funded entirely by fees charged to the grain and warehousing industries. Fees are collected for grading and sampling grain and licensing and examining public warehouses. In fiscal year 1985, the Department collected over \$4.7 million in fees and also expended over \$4.7 million. Salaries and wages accounted for over 75 percent of the Department's expenditures. The table on the next page summarizes the Department's sources and uses of funds for fiscal years 1982 to 1985.

KANSAS GRAIN INSPECTION DEPARTMENT

Sources and Uses of Funds

	Fiscal Year			
	<u>1985</u>	<u>1984</u>	<u>1983</u>	<u>1982</u>
Sources of Funds:				
Beginning Fund Balance	\$2,154,872	\$1,929,757	\$1,683,291	\$1,984,300
Fee Fund Revenues	<u>4,731,514</u>	<u>4,806,184</u>	<u>4,941,488</u>	<u>3,867,539</u>
Total Sources of Funds	\$6,886,386	\$6,735,941	\$6,624,779	\$5,851,839
Uses of Funds:				
Salaries and Wages	\$3,693,479	\$3,444,755	\$3,560,348	\$3,556,820
Contractual Services	674,268	608,951	561,666	495,781
Commodities	30,517	31,163	23,807	32,153
Capital Outlay	40,260	11,988	44,139	31,046
Non-Operating Expenditures(a)	<u>336,125</u>	<u>484,212</u>	<u>505,062</u>	<u>52,748</u>
Total Uses of Funds	<u>\$4,774,649</u>	<u>\$4,581,069</u>	<u>\$4,695,022</u>	<u>\$4,168,548</u>
Ending Fund Balance	<u>\$2,111,737</u>	<u>\$2,154,872</u>	<u>\$1,929,757</u>	<u>\$1,683,291</u>

(a) Remittance of user fees collected by the Kansas Grain Inspection Department for the federal Grain Inspection Service.

**What Steps Has the Grain Inspection Department
Taken to Implement the Recommendations
of the 1982 Performance Audit?**

To answer this question, the auditors reviewed the Grain Inspection Department's policies and procedures for licensing and examining grain warehouses and enforcing the Public Warehouse Laws. They analyzed samples of license applications and examination records and accompanied Department employees on two warehouse examinations to determine if these stated procedures were being followed. Finally, the auditors reviewed statutes and regulations and compared current procedures to those in place during the 1982 audit. Although the Department's activities include inspecting and grading grain in addition to regulating warehouses, the 1982 audit report dealt only with the Warehouse Division. Therefore, the first part of this audit concentrated only on the activities of that Division.

The Warehouse Division is responsible for enforcing the Public Warehouse Laws, which were enacted by the Legislature in 1907. This legislation acts to protect farmers who store grain in a public warehouse or elevator by regulating the practices of warehouse operators. The work of the Warehouse Division comprises three main activities: annual licensing of warehouses, periodic

examination of warehouses, and enforcement of the Public Warehouse Laws. Legislative concerns about the Department's effectiveness in carrying out these functions led to the first performance audit in 1982. In that audit report, the Legislative Division of Post Audit made recommendations in four main areas:

- improving licensing procedures
- improving financial protection for grain producers
- improving examination procedures
- improving enforcement

A number of these recommendations required changes in State law or regulation. Others required action only by the Grain Inspection Department. Generally, many of the 1982 audit recommendations requiring changes in State law or regulation have been implemented. However, in some cases the Department is apparently not in full compliance with those new laws. The auditors also found that the Department has implemented some of the recommendations directed toward it, although other recommendations have not been implemented at all or have been only partially implemented. The following sections will discuss the Department's progress in implementing the 1982 recommendations over the last three years. A complete listing of those recommendations, along with a summary of legislative and agency actions taken, can be found in Appendix A.

Recommendations for Improving Licensing Procedures

State law requires that anyone operating a public grain warehouse must have a license. No license is required if a warehouse owns all the grain it stores, but any warehouse that stores grain for someone else must have a license. Public warehouses have a choice of obtaining State or federal licensing. As of January 1, 1985, 573 of the State's 704 grain warehouses had State licenses; the remainder were federally licensed.

For State-licensed warehouses, K.S.A. 34-230 requires that the license be renewed each year. The warehouse operator is required to submit a license application and financial statement to the Grain Inspection Department. Department employees then review the application for completeness of information and sufficiency of net worth and insurance coverage. Based on the information provided in the application and financial statements, the Department computes the required amount of performance bond. The bond must be obtained, and the license fee paid, before an operating license is issued to the warehouseman. The first set of recommendations made in the 1982 audit report dealt with this licensing process. These recommendations, and the extent to which they have been implemented, are summarized in the table on the following page.

Recommendations for Improving Licensing Procedures

<u>1982 Report Recommendation</u>	<u>Recommendation Implemented?</u>
1. Seek a change in State regulations to require that financial statements be prepared in accordance with generally accepted accounting principles.	Yes
2. Seek a change in State regulations to require that financial statements be accompanied by an audit or review report of a certified public accountant.	Yes
3. Seek a change in State regulations to require that license applications be submitted within 90 days of the date of the accompanying financial statements.	No
4. Develop specific tests and analyses of the financial information submitted by warehouses.	Partially
5. Review the adequacy of insurance coverage before issuing a license.	Yes

As the table shows, three of the five recommendations for improving licensing procedures have been fully implemented. The first two recommendations listed in the table were implemented by amendments made in 1983 to the Public Warehouse Laws. However, the Department is not always making warehouses comply with the amendment requiring that financial statements be prepared in accordance with generally accepted accounting principles. In addition, one recommendation has been only partially implemented, and the remaining recommendation has not been implemented.

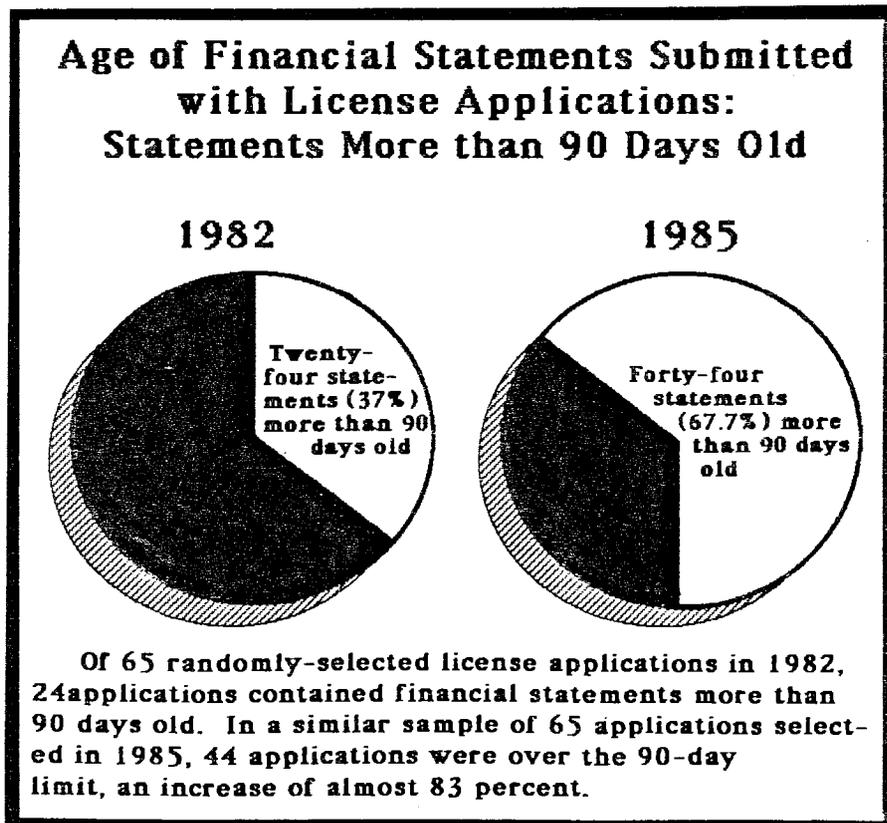
The Department has accepted a number of financial statements that do not meet the requirements of State law. As recommended in the 1982 audit report, the 1983 Legislature amended K.S.A. 34-228 to require that the financial statements submitted with warehouse applications include a current balance sheet, income statement, statement of retained earnings, and statement of changes in financial position. These changes were designed to standardize the information supplied on warehouse applications and provide more complete financial information to the Department.

The Department has communicated this requirement to State-licensed warehouses, and it appears that many of the warehouses have complied. However, when the auditors reviewed a random sample of 65 of the 564 license applications processed by the Department in fiscal year 1985 they found that nine applications, or 13.8 percent, lacked at least one of the four required

parts. The most frequent omission identified was the statement of retained earnings. In addition, five of the statements reviewed were presented in ways that were not in accordance with generally accepted accounting principles. Those cases generally involved financial statements prepared on an income-tax basis.

The Department does not require that license applications be submitted within 90 days of the date of the financial statements. Because the financial condition of a warehouse may change rapidly, it is important for its financial statement to be as current as possible. The 1982 audit recommended that the Department seek a change in State regulations to require that license applications be submitted within 90 days of the end of a warehouse's fiscal year. At that time, 37 percent of the 65 license applications reviewed contained financial statements that were more than 90 days old. During the current audit, the auditors found that the Department has not adopted any formal rules or regulations regarding the 90-day limit. K.S.A. 34-228 (b) now requires that the financial statements submitted must be current at the time of submission, but the term "current" is not defined.

Department officials did indicate they are now asking for updated financial statements if the ones submitted with the application are over 90 days old. However, in reviewing their sample of applications processed during 1985, the auditors discovered that 44 of 65 applications, or 68 percent, contained financial statements older than 90 days. The average late statement in the sample was about 14 weeks beyond the 90-day limit. As the accompanying pie chart indicates, the number of financial statements more than 90 days old has increased substantially since 1982.



Although the Department has begun some simple ratio analyses of the financial statements submitted by warehouses, it makes little or no use of the information. The previous audit report recommended that the Grain Inspection Department analyze the financial statements submitted by warehouses to help evaluate the warehouses' financial health. This information could provide indications that an elevator is on a weak financial footing. For example, the 1982 report noted that sometimes the first signal a warehouse was in financial trouble was its difficulty in obtaining a bond from a bonding company. The report further pointed out that by conducting its own analyses of licensees' financial conditions, the Department would be able to independently assess their ability to meet their obligations.

The 1982 report specifically recommended that the Department use financial ratios in its evaluation of warehouses. For example, a warehouse's information could be compared with standards, and the changes in a warehouse's condition over several years could be analyzed. The Department has partially implemented this recommendation by calculating and recording the ratio of total assets to total liabilities and the ratio of current assets to current liabilities. However, the Department does not use or analyze these ratios. In some cases, the ratios are also calculated incorrectly. For the 65 applications reviewed, the auditors examined a total of 124 ratios recorded by the Department. Of these 124 ratios, 11 were calculated incorrectly. Some ratios appeared to have been calculated backwards, and some were stated as negative numbers when none should have been less than zero.

Licensing section staff told the auditors that the reason why these ratios are not used in making licensing or bond requirement decisions was that the Department might be liable for lawsuits if it denied a license to a company that had sufficient net worth. Staff members reported that the ratios were consulted occasionally, but not on a routine basis. No comparison of individual ratios to standard or normal ratios takes place.

Although ratio analyses will not always indicate when financial or management problems exist, ratios can be used as one indicator of the condition of a business. For example, the ratio of current assets to current liabilities was consistently below standard for five of the eight elevators that failed between 1983 and 1985. While a two to one current ratio is considered standard, one failed elevator had an average current ratio of .4 between 1980 and 1983.

The 1982 report further recommended that the Department develop a plan for ensuring that its staff had the expertise needed to develop and make use of the financial information submitted by the licensees. The auditors determined that the employee responsible for the licensing section had taken a college-level beginning accounting course. However, a beginning accounting course may be insufficient training for detailed analyses of warehouse financial statements.

Recommendations for Improving Financial Protection for Grain Producers

State law requires that a public grain warehouse maintain an established net worth. Net worth is the difference between a warehouse's total assets and

its total liabilities. If a warehouse is not able to meet the net worth requirement, the Grain Inspection Department increases the size of the required performance bond to make up the difference. In 1982, State law required warehouses to maintain a net worth of 10 cents per bushel of licensed capacity up to \$100,000. The net worth requirement was based on storage capacity and no minimum net worth was required. The 1982 audit concluded that this practice was not protecting grain producers against losses. Two recommendations for improving the financial protection offered to producers were made in that report. These recommendations, and their subsequent status, are summarized in the table below.

Recommendations for Improving Financial Protection For Grain Producers	
<u>1982 Report Recommendation</u>	<u>Recommendation Implemented?</u>
1. Seek a change in State regulations to require that warehouses have a minimum net worth. Any difference between that minimum net worth and the net worth of a particular warehouse would be made up through an increase in bond.	Yes
2. The Legislature should consider raising bond requirements for elevators.	No

As the table shows, the first recommendation, to establish a minimum net worth, was implemented by the 1983 Legislature. K.S.A. 34-228 now requires all warehouses to have a net worth of 20 cents per bushel of capacity, with a minimum net worth of \$25,000. During their review of the 1985 license files, the auditors noted that in all cases the correct net worth was required of the applicant, and the additional bond was correctly requested and obtained in all cases where extra bonding was required. For the second recommendation, no action has been taken to raise bond requirements, and the Grain Inspection Department does not support that action. The auditors also reviewed the financial losses incurred by producers in the eight warehouse failures between 1983 and 1985. Producers will apparently incur some loss in three of those failures. A listing of the estimated amount of loss in each of the eight cases can be found in Appendix B.

Bond requirements for grain elevators have not been raised, and the Department does not agree that they should be. State law specifies the formula to be used in computing the size of a warehouse's required performance bond. The required bond amount is obtained by multiplying the closing cash price per bushel (less \$.25) of No. 2 hard ordinary wheat in Kansas City on a given day times 15 percent of the warehouse capacity, up to \$200,000. After the first

\$200,000 of bond, the cash price less \$.25 is multiplied by one percent of the warehouse capacity in excess of the capacity used to compute the first \$200,000 of the bond. To provide more protection for producers, the 1982 audit recommended raising the requirements to 25 percent of capacity up to a \$300,000 bond, and 1¼ percent of the capacity in excess of the capacity used to compute the first \$300,000 of bond. No legislation to implement this recommendation has been enacted.

During the current audit, the Grain Inspection Department indicated that it did not agree with this recommendation. According to the Department, increasing the formula and resulting bond requirements would make bonding requirements in Kansas more stringent than the federal requirements. Department officials think this change would cause more elevators to obtain licenses from the federal government. The State's bond requirements are compared to federal requirements in the box below. Also, the cost of obtaining various amounts of bonding in Kansas is shown in the table on page 10.

COMPARISON OF FEDERAL AND STATE BOND REQUIREMENTS

A performance bond provides another recourse for a creditor of a warehouse, such as a farmer who has stored his grain, when a warehouse fails. Bonding requirements for both federal and State licensure are based on the size of a warehouse, but different formulas are used to calculate the bond amounts.

BONDING BY KANSAS GRAIN INSPECTION DEPARTMENT

The required performance bond is computed by multiplying the cash price of a bushel of wheat, less 25 cents, times 15 percent of a warehouse's capacity up to \$200,000. After a \$200,000 bond is required, the cash price (less 25 cents) is multiplied by one percent of the warehouse's capacity in excess of the capacity used to calculate the first \$200,000 of the bond. Minimum bond is \$10,000; there is no maximum.

BONDING BY THE U.S. DEPARTMENT OF AGRICULTURE

The required performance bond is computed by multiplying 20 cents per bushel times the first million bushels of licensed capacity; 15 cents per bushel for the next one million bushels; and 10 cents per bushel for all licensed capacity over two million bushels. Minimum bond required is \$20,000; maximum is \$500,000.

The following table shows how the differences between these two formulas affect warehouses of various capacities:

<u>Capacity (bushels)</u>	<u>Kansas Bonding</u>	<u>Federal Bonding</u>	<u>Difference</u>
500,000	\$205,965	\$100,000	\$ 105,965
1 million	225,965	200,000	25,965
2 million	265,965	350,000	(84,035)
3 million	305,965	450,000	(144,035)
4 million	345,965	500,000	(154,035)
5 million	385,965	500,000	(114,035)
10 million	585,965	500,000	85,965
20 million	985,965	500,000	485,965

As the table shows, the warehouses with capacities in the range of 2-5 million bushels have the most incentive, with respect to bonding requirements, to obtain State licenses. For elevators with more or less capacity, federal bond requirements are lower.

Bond Costs for Warehouses

<u>Warehouse Capacity (bushels)</u>	<u>Kansas Bond Required*</u>	<u>Cost of Bond</u>
100,000	\$ 57,000	\$ 127.50
250,000	142,500	235.00
500,000	205,965	313.75
1,000,000	225,965	338.75
10,000,000	585,965	788.75
20,000,000	985,965	1,288.75

* For fiscal year 1985.

Recommendations for Improving Examination Procedures

In addition to licensing warehouses, the Department also periodically reviews the operations of each licensed facility. During these examinations, the Department's warehouse examiners determine whether elevator records are adequate, whether enough grain is on hand, and whether various aspects of the law are being complied with. Effective July 1, 1985, each State-licensed warehouse is to be examined at least three times every two years, with a minimum of one exam per year. The box on the next page provides a brief summary of the Department's examination process and describes the various records reviewed by the examiner.

The 1982 audit report made five recommendations for improving these examination procedures. To determine the extent to which these five recommendations were implemented, the auditors reviewed examination reports and accompanied Department examiners on their visits to the warehouses of two licensees. The table below summarizes the recommendations made in this area.

Recommendations for Improving Examination Procedures

<u>1982 Report Recommendation</u>	<u>Recommendation Implemented?</u>
1. Test the mathematical accuracy of individual settlement sheets.	Yes
2. Trace scale tickets to daily position records and test numerical accuracy of scale tickets.	Yes
3. Test accuracy of daily position records and trace daily position transactions to source documents.	Yes
4. Test "outbound" scale tickets as well as "inbound" tickets.	No
5. Increase the number of scale tickets tested in larger capacity warehouses.	No

As shown in the table, the Department has implemented three of the five recommendations but has taken no action on the last two recommendations.

SUMMARY OF ON-SITE EXAMINATION PROCEDURES GRAIN INSPECTION DEPARTMENT

The Warehouse Division of the Grain Inspection Department has 16 authorized positions for grain warehouse examiners. As of June 30, 1985, 13 of these 16 positions were filled. Two of these examiners are employed in the Department's central office in Topeka, and the remaining 11 examiners are primarily responsible for conducting on-site examinations of warehouses across the State. The procedures used during those examinations are summarized below.

Measuring the Grain

The examiner physically measures the grain to determine how much is on hand. During the measurement process, the examiner notes any infestation, deterioration, or threat to the condition of the stored grain.

Determining the Accuracy of Warehouse Records

The amount of grain actually on hand is compared with the amount indicated on warehouse records. Warehouses use various kinds of records to keep track of the flow of grain in and out of the warehouse. These records include the following:

- Scale tickets.** Scale tickets record each individual transaction of grain shipped into and out of the warehouse. "Inbound" scale tickets are issued to farmers who bring their grain to the warehouse; "outbound" tickets record shipments from the warehouse.
- Warehouse receipts.** These receipts can be used to obtain loans on grain. They indicate that the warehouse is storing a certain amount of grain that is credited to a particular account.
- Settlement sheets.** These are individual storage records are maintained for each person who deposits grain. They show the cumulative record of scale tickets and warehouse receipts for each depositor at the warehouse.
- Daily position records.** These records show, on a daily basis, all grain handled by the warehouse. They are created from the daily record of scale tickets.
- Monthly stock reports.** Warehouses create these reports from the daily position records and submit them to the Grain Inspection Department each month. During on-site examinations, they are checked against records at the warehouse.

Reviewing the Adequacy of Insurance

Stored grain must be insured for its full market value against casualty loss. The amount of insurance is verified and is checked for sufficiency.

Inspecting Safety and Sanitation Conditions

The examiner reviews safety and sanitary conditions at the warehouse.

The Department does not agree that testing of "outbound" scale tickets is necessary. "Outbound" scale tickets record grain taken out of the warehouse and "inbound" tickets record grain brought into a warehouse. During warehouse examinations, the Department tests "inbound" tickets because those provide the first formal documentation of the receipt of grain. The 1982 report recommended that the Department test "out bound" scale tickets as well, because a warehouse's estimates of grain on hand is no more accurate than the scale tickets from which it is calculated. However, the Grain Inspection Department

does not think it is necessary to test "outbound" tickets because only "inbound" scale tickets are source documents for establishing a warehouse's grain liability.

The Department has not increased the sample sizes of the records tested for larger-capacity warehouses. Increased testwork is important because an elevator with a large capacity is more likely to have a larger number of grain transactions. Currently--and at the time of the 1982 audit--the Department's procedures call for the examiner to select and tract a minimum sample of 20 scale tickets to the corresponding settlement sheets. This procedure confirms that all grain storage transactions have been posted to the accounts of the individual producers.

Department officials say they are doing larger samples in some cases. However, the Department has apparently not established formal guidelines for determining sample sizes. The auditors accompanied two Department examiners on warehouse examinations and found that each examiner selected a sample of 20 to 25 tickets. Both examiners said there were no formal guidelines for determining sample size beyond that number based on the capacity of the warehouse or the number of transactions.

Basing the number of scale tickets tested on the warehouse's capacity, rather than an absolute minimum as is now the case, would probably result in larger number of tickets being reviewed at bigger warehouses. For example, for a 5 million bushel capacity warehouse which had 1,500 transactions (scale tickets written) since its last exam, a Department examiner might review as many as 75 tickets, or five percent of the total, rather than the currently required 20.

SUMMARY OF THE GRAIN WAREHOUSING PROCESS

The movement of grain from the field to the processor or other buyer begins with the grain harvest. In the case of winter wheat, the most commonly produced and stored grain in Kansas, harvest occurs in June and July. Other crops are harvested at other times of the year, some as late as mid-winter. If the producer--the farmer--has storage facilities, he may elect to store his own grain. However, adequate storage facilities with apparatus to turn and condition the grain are costly, and many producers use commercial elevators.

After the grain is harvested, it is carried by trucks to a grain elevator, or warehouse. It is dumped from the truck, and deposited in an elevator bin with other grain of the same kind. The farmer can sell his grain to the elevator or only store it there. If the grain is only stored at the elevator, the elevator charges the farmer for storage. Elevators' storage charges for grain must be approved by the Grain Inspection Department. Typical storage fees for grain are about eight-hundredths of a cent per bushel per day. These charges may be periodically billed to the owner of the grain, or they may be accumulated and deducted from the amount of the grain which is eventually returned to the owner.

Recommendations for Improving Enforcement

The Grain Inspection Department has the authority to require public warehouses to correct conditions that are not in compliance with the Public Warehouse Laws. For warehouses that fail to comply with these laws, the Department can conduct special examinations and suspend or revoke licenses.

In more serious cases, the Department can take possession of a warehouse or seek the appointment of a receiver if the warehouse goes bankrupt.

The 1982 audit report concluded that the Department generally had the enforcement tools it needed; it just did not use many of them. Six recommendations for enhancing enforcement activities were made in the previous report. Those recommendations, along with the Department's actions in this area since 1982, are summarized in the table below.

Recommendations for Improving Enforcement	
<u>1982 Report Recommendation</u>	<u>Recommendation Implemented?</u>
1. Require examiners to document apparent violations of the Public Warehouse Laws.	Yes
2. Require examiners to document their follow up on prior deficiencies.	Yes
3. Require special follow-up examinations if severe or recurring problems are noted.	Partially
4. Take stronger actions when appropriate.	Partially
5. Review completed examinations more extensively, and begin on-site evaluation of examiners.	Partially
6. Amend the Warehouse Act to provide appropriate penalties for maintaining false or duplicate records.	Yes

As the table shows, three of these six recommendations have been fully implemented. Department examiners are now required to document violations of the Public Warehouse Laws and follow up on prior deficiencies while conducting warehouse examinations. Also, as of July 1, 1985, it is a class D felony to make false public warehouse financial records, statements, and reports. The Department indicated it has implemented the three remaining recommendations, but in some cases the auditors were not able to find documentation that fully supported that claim.

The Department is making an effort to re-examine problem warehouses more frequently. The 1982 audit report noted that the Department had sometimes failed to follow up sufficiently on warehouses where recurring or severe problems were noted. Follow-up examinations in problem cases can help to catch problems early and possibly prevent some warehouse failures. The Department says it is now expediting these follow-up examinations and has instituted a system for reviewing the files of problem warehouses more frequently.

The Department has established a suspense file which allows Department staff to review problem files at predetermined intervals. During the audit fieldwork, that suspense file included 19 warehouses, or 3.4 percent of all public warehouses with State licenses on June 1, 1985. Department records indicate that 16 of these 19 warehouses had been in the suspense file at least since January 1, 1984. The Department inspected these 16 warehouses an average of 3.18 times during the 18-month period from January 1984 through June 1985. In other words, these 16 problem warehouses were examined about twice a year. For the 65 random warehouses reviewed, the Department examined each warehouse an average of 1.6 times a year. Thus, the Department is conducting more examinations of the warehouses identified as problem warehouses. The auditors were not able to determine if all warehouses with recurring problems are included in the Department's suspense file.

The auditors were unable to document the Department's assertion that it is taking stronger enforcement actions. The 1982 report recommended that the Department begin taking stronger enforcement actions, including assessing fines and penalties and suspending or revoking licenses. During this audit, Department officials indicated that they have begun taking such actions when appropriate. However, the Department does not maintain central records of enforcement actions taken, and the auditors were unable to document this assertion. The Department did report that for fiscal year 1985, 15 warehouses were charged for 47 special examinations involving severe or recurring problems or bond surveillances.

**Warehouse Financial Operations:
An Example**

Public grain warehouses buy and sell grain of their own and store grain for producers. Some elevators also sell farm supplies and process feed. Annual proceeds from these sales and storage fees could total about \$8 million for an elevator with a capacity of two million bushels. The elevator might also have sales costs and operating expenses of about \$7.75 million. That would leave the company an income of \$250,000 for the year.

With a capacity of two million bushels, this elevator would be required to pay an \$850 annual license fee to the Grain Inspection Department. The warehouse would also have to obtain a bond for \$265,965, which would cost about \$390.

Of 65 random licensees sampled, six had failed to take the corrective measures, ordered on at least one previous exam. These corrective measures included such things as replacing deficiencies in stored grain from company-owned stock, or making repairs to the warehouse itself. However, the Department did not proceed to take stronger actions in any of those six cases. The auditors also noted that the Department sometimes seemed reluctant to take stronger enforcement actions, despite chronic problems. The case of one such elevator is profiled on page 15.

The Department now plans to conduct on-site evaluations of the warehouse examiners' performance every other year. The 1982 audit recommended that the Department institute a systematic, on-site evaluation of the examiners. The Department conducted such a review in calendar year 1983, but did not do one in 1984. Department officials are now beginning to conduct on-site evaluations for 1985, and say they plan to do so in alternating years. The 1982 report also recommended that the chief examiner should review examinations

more thoroughly, to ensure that examinations were being conducted uniformly and that the Warehouse Laws were being consistently enforced. The auditors were told that the Chief Examiner now reviews examination records for warehouses on the Department's suspense listing.

PROBLEM WAREHOUSES: AN EXAMPLE

One of the warehouse files reviewed by the auditors contained an example of the Department's apparent unwillingness to actually suspend or revoke a license. This warehouse company had consistent compliance problems: a letter to the operator from the Director of the Grain Inspection Department, dated June 24, 1984, cited "under-measurements, deteriorated grain and errors in your records." The auditors review of the file showed that the company had four examinations between January 1984 and June 1985. Each time, the warehouse had less grain on hand than its records indicated. In addition, the company had been oversold (a violation of State law) three times in the same period.

The letter from the Director further stated: "...I have seen instances where concerns were closed out in cases such as you present here." The operator was directed to cover shortages totaling 27,438 bushels of grain within 24 hours of receipt of the letter. The letter concluded: "In the event our Warehouse Examiner finds you have not complied with the requirements of this letter, you will be notified immediately of your suspension as a licensed warehouse."

The Department's follow-up examination was not conducted until July 11th, 17 days later. Although the undermeasurements were corrected, there was no mention in the examiner's follow-up report as to whether the correction was made within the 24-hour limit imposed in the letter.

Undermeasurements and other examination deficiencies were not the only problems plaguing this warehouse. Because of the company's poor financial position, its bonding company refused to renew its warehouse bond in February 1985. At that time, the company's ratio of current assets to current liabilities was less than two to one: where the company's current assets should have been at least twice their current liabilities, they were less than half. Because the Department does not use ratio analysis in its licensing decisions, the company was issued a license after being required to provide an additional bond of \$40,200, based upon insufficient net worth.

Finally, in the process of granting the license, the Department may have violated State law. The license application, as originally submitted, contained only a balance sheet and not a complete financial statement as required by K.S.A. 34-228(b). To fully comply with the law, the Department should not have issued a license until the company provided a full financial statement prepared in accordance with generally accepted accounting principles. According to Department staff, the Department issued a license so that the company could continue to operate. The Department did not actually mail the license to the company; rather, the license was held in the Department's file pending receipt of the complete financial statement. According to Department staff, keeping the license would act as a motivator to the company, encouraging it to submit the complete statement as soon as possible. The warehouse finally submitted the required financial statements in late June 1985. As of July 30, 1985, the Department had not mailed the license because the company had not obtained the additional \$40,200 bond. If the company operated without possession and display of its current license between April and July 1985, the warehouse was in violation of K.S.A. 34-230(e) during that time. Violation of that statute is a class C misdemeanor.

Conclusion

The 1982 audit report made numerous recommendations for improving the laws and procedures for licensing and examining public grain warehouses, enforcing the Public Warehouse Laws, and providing financial protection for grain producers. Other than the two recommendations with which the Department disagrees, testing of "outbound" scale tickets and increasing bond requirements, Department officials say they have implemented all other suggestions from the prior audit report. However, the auditors found that while some changes have indeed been made, additional improvements are needed. Most of these improvements are needed in the areas of licensing warehouses and enforcing the Public Warehouse Laws. Specific recommendations to further improve the Department's operations examined under this audit question are listed below.

Recommendations

1. To improve its licensing procedures, the Grain Inspection Department should:
 - a. Seek legislation requiring that grain warehouses submit license applications within 90 days of the end of the warehouse's fiscal year. The Department should also be given the authority to impose fines or penalties for any warehouse's failure to satisfy this requirement.
 - b. Analyze the financial data it receives from warehouses to evaluate the financial stability of applicants. Further, the Department should seek additional staff training or outside consultation as needed to assure that its staff has the expertise to evaluate the financial information.
2. To improve examination procedures and ensure that those procedures are adequate for protecting grain producers, the Department should develop formal guidelines on the number of scale tickets to be tested at elevators of various sizes. The guidelines developed should provide a sample size that is manageable yet adequate for larger warehouses.
3. To help evaluate enforcement procedures, the Department should maintain a complete record of enforcement actions taken against warehouses, and the basis for each action taken. Because no such record now exists, it is difficult for the Department or the Legislature to determine if enforcement of the Public Warehouse Laws is adequate.

Is the Department, In Carrying Out Its Mandated Activities, Complying With All Applicable Laws and Regulations Governing the Use of State Property and Resources?

In addition to the Grain Inspection Department's implementation of the previous audit recommendations, the auditors also examined the Department's compliance with State laws and regulations governing the use of State property and resources. The auditors reviewed the Grain Inspection Department's policies and procedures in a number of areas. They examined a variety of personnel transactions which occurred during fiscal year 1985. They also reviewed samples of travel and subsistence vouchers and Central Motor Pool vehicle logs. Finally, the Department's telephone usage and lease of office space were reviewed.

Generally, the auditors found that the Department is in compliance with State laws and regulations governing the use of State property and resources. However, in the area of personnel transactions, the auditors noted that the Department's documentation and exit interview procedures could be improved. In reviewing travel expenditures, the auditors determined that some motor pool vehicles permanently assigned to the Department were not meeting their minimum mileage requirements. Finally, the auditors found that the Department had no formal telephone policy until July 1985 and that the cost of the Department's leased office space appeared only slightly higher than the average for State agencies. These findings will be discussed in more detail in the following sections.

Personnel and Timekeeping Practices Generally Comply With State Requirements, But Agency Recordkeeping is Sometimes Not Complete

In the area of personnel practices, the auditors reviewed a sample of fiscal year 1985 appointments, terminations, and associated personnel transactions. A total of 40 appointments were examined, representing 35 percent of the total transactions during the year. The sample contained 15 classified full-time positions, 20 temporary positions, and five emergency positions.

For each appointment in the sample, the auditors reviewed the Department's actions in filling the position, including the recruitment and evaluation of the applicants, and the minimum qualifications, probationary period, and performance evaluations of each person hired. In addition, for permanent employees, the auditors reviewed the Department's actions relating to the separation of the employee who previously held the position. The results of the auditors' review showed that most of the sampled personnel transactions were handled properly. The exceptions were in the areas of maintaining interview records, posting vacancy announcements, conducting exit interviews, and documenting hours worked by temporary employees.

Employment interview records were not maintained in all cases. None of the employee files in the sample contained any record of the interview proceedings or the reasons for hiring. Although this documentation is not required by State regulations, it is recommended by the State Equal Employment Opportunity Office to protect the agency in the event of an affirmative

action complaint. In addition, this documentation is needed by the State Equal Employment Opportunity Office to verify the Department's compliance with affirmative action requirements. Some supervisors do maintain a list of standard questions for all applicants, but such sketchy records would not afford much protection to the Department in the event of a complaint.

The Department was not able to provide documentation that position vacancies had been posted within the agency. K.A.R. 1-6-2 requires that all position vacancies be posted within the agency, except for certain specified types of appointments and in cases where the Director of Personnel Services determines that it is not necessary and authorizes the agency to make an appointment without providing notice of the vacancy. The purpose of this requirement is to ensure that employees can compete for positions along with other applicants. The posting must be made even if the agency requests a certified register, or believes that no interested or qualified applicants are available within the agency. Internal postings are not required for vacancies to be filled by temporary and emergency appointments.

The auditors attempted to review the Grain Inspection Department's posted vacancy announcements, but the agency's personnel clerk could not locate such a file. The personnel clerk had been employed by the agency less than two months when the audit field work was conducted, and did not know whether the agency had failed to post the required notices or had simply failed to maintain a record of the postings. The auditors determined that the Department had not gotten approval from the Director of Personnel Services to fill any permanent positions without posting vacancy notices. Therefore, if the position vacancies were not posted internally, all the permanent appointments were made in violation of State regulations. Along with its response to Legislative Post Audit's draft report, the Grain Inspection Department provided documentation that some position vacancies had been posted.

Actions relating to persons who left positions appeared to be in overall compliance with State laws and regulations, but exit interview procedures could be improved. For the 15 classified permanent positions in their sample, the auditors reviewed the actions relating to the separation of the previous incumbent. Three of the current employees had no predecessors; their positions had been reallocated. Two current permanent employees had replaced temporary or emergency personnel. For the 10 previous incumbents analyzed, one former employee's file did not contain records of an exit interview. An exit interview for each separating employee is required by K.A.R. 1-9-20.

The personnel files of the nine other former employees sampled did contain documentation of exit interviews. However, in all cases the exit interview was conducted by the employee's supervisor. Officials of the Division of Personnel Services report that they strongly discourage agencies from using employees' supervisors to conduct exit interviews. One reason is that many employees--even those who are about to leave the agency--are reluctant to give negative or uncomplimentary feedback to their supervisor. The exit interview process is important because, if done properly, it provides potentially useful information on employee concerns and problems within the agency.

Some temporary workers worked more than the 999 hour maximum allowed for the year. The auditors reviewed the records for a sample of 20 temporary

and five emergency workers. The five emergency appointments were all terminated within their maximum work limits, and were otherwise handled in accordance with State regulations. However, two of the 20 temporary employees were inadvertently allowed to work more than the 999 hours prescribed by State regulations. The two workers put in a combined total of 86 hours over the limit.

Local supervisors handle timekeeping for temporary employees, who generally work at grain inspection offices outside of Topeka. When the excessive hours worked by the two employees in the auditors' sample were pointed out to the Department, officials sent a memo to all supervisors reminding them of their responsibility to see that the 999-hour limit is observed. However, it appears that no central review of timesheets is conducted to check for temporary or emergency appointment time limits. Officials from the Division of Personnel Services indicated that an edit in the KIPPS system will generate a notice to agencies that employ any temporary worker for more than 999 hours. However, that edit is purely informational and does not prevent the employee from being continued on the agency payroll indefinitely. Division of Personnel Services officials are proposing enhancements that would give the KIPPS system more power to enforce the temporary and emergency limits.

The Department's Handling of Travel and Subsistence Matters Was Generally in Compliance With the Applicable Requirements

The Grain Inspection Department's total expenditures for travel and subsistence during fiscal year 1984 were \$221,205. The auditors reviewed a sample of 30 fiscal year 1984 travel vouchers totaling \$16,100 to determine if travel and subsistence payments were handled in compliance with State rules and regulations. They reviewed each voucher for mileage, dates, destination, and reason for travel. The auditors found that these payments generally complied with State regulations, but some vehicles permanently assigned to the Department are not meeting the minimum mileage requirements.

The Department's use of permanently assigned motor pool vehicles was appropriate, but some vehicles are not meeting their minimum mileage requirements. The Department has a total of 32 permanently assigned motor pool cars, vans, and pickup trucks. These vehicles are primarily used by the agency's field personnel, although one car is assigned to the Department's central office in Topeka. The Department of Administration requires that permanently assigned vehicles in Shawnee County be driven at least 18,000 miles a year, or about 1,500 miles each month. Permanently assigned vehicles based outside Shawnee County must be driven 15,000 miles a year. Of the 32 vehicles permanently assigned to the Grain Inspection Department, the auditors found that five vehicles did not meet the minimum mileage requirements. For the 12-month period from June 1984 through May 1985, the auditors determined that these five vehicles averaged nearly 2,000 miles per year less than required.

The Department's Telephone Procedures Were Generally In Compliance with State Regulations, But Some Minor Problems Were Noted

To determine whether the Department's telephone usage was appropriate, the auditors examined the Department's policies and procedures relating to use

of the KANS-A-N system. They paid special attention to the Department's internal auditing of telephone bills. A sample of telephone billings was analyzed, along with records showing any reimbursement received from employees making personal calls. Finally, the auditors followed up on numerous calls made to eight telephone numbers during the month of February, as identified during Legislative Post Audit's performance audit, Reviewing Controls Over the KANS-A-N System. In sum, the auditors found that the Department's procedures for monitoring telephone usage were adequate, but the Department did not have written policies governing the use of KANS-A-N and employees were not well informed of the Department's telephone policy.

The Department's procedures for monitoring telephone usage appeared to be adequate, but an official policy on phone use was only recently implemented. Each employee authorized to make calls must keep a monthly log of the long distance calls made. The auditors reviewed these employee telephone logs for April 1985 and determined that the calls made appeared to be reasonable and were related to the conduct of State business. They also determined that the 116 calls made to eight particular telephone numbers during February 1985 appeared to be related to State business.

However, as of July 1, 1985, the Department did not have any written procedures governing telephone usage. Agency personnel received their information on the correct use of the KANS-A-N system through verbal instructions only. Although the Department's periodic auditing of the telephone billings was thorough, in some cases the officials reviewing the logs and billings did not seem to know what the Department's policy was on personal phone calls. However, effective July 18, 1985, the Grain Inspection Department adopted a written policy prohibiting personal use of the KANS-A-N system except in emergency situations.

The Cost of the Department's Office Space is Slightly Higher Than Comparable Space For Other State Agencies

The Grain Inspection Department leases office space in eight cities across the State. For fiscal year 1986, the Department is requesting approximately \$158,000 to lease office space, including \$40,000 to lease space for its central office in Topeka. To determine if these expenditures were reasonable, the auditors compared the cost of the Department's central office space with the cost of similar State-leased space in Topeka. They also reviewed the cost of office space for the Department's field offices.

Overall, they found that the Department's central office space appears to be only slightly more expensive than similar State offices in Topeka. For the Department's field offices, the office space leased in Kansas City was the most expensive, while the space leased in Dodge City was the least expensive. The total lease cost and square feet of space leased at each location is summarized in the following table.

Office Space Leased by the Grain Inspection Department

Fiscal Year 1985

<u>Location</u>	<u>Total Square Feet</u>	<u>Annual Lease</u>	<u>Utilities</u>	<u>Custodial</u>	<u>Total Annual Cost</u>	<u>Cost per Square Foot</u>
Topeka (central office)	5,659	\$39,613	paid	\$2,160	\$41,773	\$7.38
Atchison	1,350	5,400	\$1,557	--	6,957	5.15
Colby	1,000	6,600	1,229	--	7,829	7.82
Dodge City	1,295	5,802	paid	--	5,802	4.48
Hutchison	4,000	15,600	3,710	--	19,310	4.82
Kansas City	3,280	31,160	paid	paid	31,160	9.50
Salina	2,178	13,150	paid	paid	13,150	6.03
Topeka	2,696	13,482	3,419	--	16,901	6.26
Wichita	3,048	23,409	4,004	--	27,413	8.99

The Grain Inspection Department's central office building in Topeka is leased to the Department of Administration, which in turn sublets space to the Grain Inspection Department. In addition, the Department leases a garage attached to the building for \$25 a month. The lease term is 30 months, and it will expire May 14, 1986. Thereafter, the Department may move to the State Office Building, or may remain in its present quarters, depending on plans presently being formulated by the Division of Architectural Services.

Conclusion

The auditor's review of the Department's office procedures and adherence to laws and regulations concerning the use of State property and resources showed that procedures in the area of personnel, travel expenditures, telephone usage and office space were generally in compliance with State laws and regulations. A few permanently assigned motor pool vehicles are not meeting their minimum mileage requirements, but the shortfall is not great.

The most significant area of concern is personnel recordkeeping. Although the Department's personnel policies and practices and its handling of most types of personnel actions generally comply with State and federal requirements, there are specific areas in which the Department's practices need improvement. In particular, timekeeping records and some hiring procedures are incomplete or weak. In each of these areas, the Department should take steps to bring the agency into full compliance.

Recommendations

To improve personnel procedures and comply with State laws and regulations, the Grain Inspection Department should:

1. Ensure that all position vacancies are posted within the agency to comply with K.A.R. 1-6-2(b) and should maintain a record of those postings.

2. Maintain records of all employment interviews. A record of the interview proceedings should be prepared even if there is only one applicant for the position. The personnel officer should make all supervisors aware that documentation requirements are to be applied uniformly, as protection to both applicants and the agency.
3. Seek consultation from the Division of Personnel Services on ways to enhance the exit interview process. One possible way to make the procedure more effective might be to have all exit interviews conducted by the personnel clerk or other non-supervisory staff person, by telephone if necessary.
4. Institute central office review of the hours worked by temporary and emergency workers to assure that they are not allowed to exceed the maximums for such positions.

APPENDIX A

Implementation of the 1982 Audit Recommendations

The 1982 audit report made a series of recommendations for improving the Grain Inspection Department's operations. These recommendations addressed four areas: licensing procedures, financial protection for grain producers, warehouse examination procedures, and enforcement of State law. This appendix lists each 1982 recommendation, and indicates the extent to which it was implemented, and, if so, how the change was accomplished.

<u>1982 Recommendation</u>	<u>Implementation</u>
1. Require that financial statements be prepared in accordance with generally accepted accounting principles.	K.S.A. 34-228 amended, but Department implementation not complete.
2. Require that financial statements be accompanied by an audit or review report of a certified public accountant.	K.S.A. 34-228 amended.
3. Require that license applications be submitted within 90 days of the date of the accompanying financial statements.	Department requests, but does not require, 90-day deadline.
4. Develop specific tests and analyses of the financial information submitted by warehouses.	Department calculates and records ratios, but does not analyze the results for licensing decisions.
5. Review the adequacy of insurance coverage before issuing license.	Department now conducts on-site review of policy before licensing.
6. Require that warehouses have a minimum net worth. Any difference between that minimum and the net worth of a particular warehouse would be made up through an increase in bond.	K.S.A. 34-228 amended.
7. The Legislature should consider raising bond requirements for elevators.	Not implemented.
8. Test the mathematical accuracy of individual settlement sheets.	Implemented by Department.

<u>1982 Recommendation</u>	<u>Implementation</u>
9. Trace scale tickets to daily position records and test numerical accuracy of scale tickets.	Implemented by Department.
10. Test accuracy of daily position records and trace daily position transactions to source documents.	Implemented by Department.
11. Test "outbound" scale tickets as well as "inbound" tickets.	Not implemented; the Department says this change is not necessary.
12. Increase the number of scale tickets tested in certain areas.	Department has not developed formal guidelines for sample size.
13. Require examiners to document apparent violations of the Public Warehouse Laws.	Implemented by Department.
14. Require examiners to document their follow up on prior deficiencies.	Implemented by Department.
15. Require special follow-up examinations if severe or recurring problems are noted.	List of problem warehouses maintained and those warehouses are examined more frequently.
16. Take stronger actions when appropriate.	The Department says stronger actions are being taken; auditors could not confirm.
17. Review completed examinations more extensively, and begin on-site evaluation of examiners.	Examinations being reviewed by central office staff in a timely manner; examiners being evaluated on-site in alternate years.
18. Amended the Warehouse Act to provide appropriate penalties for maintaining false or duplicate records.	Amended by S.B. 300 (1985).

APPENDIX B

Grain Warehouse Failures in Kansas January 1983 - June 1985

Year	Company and Location	Capacity (Bushels)	Shortage (Bushels)	Estimated Financial Losses	
				Grain Producers	Bonding Companies
1983	J & H Grain Company, Inc. Thayer	168,514	5,851	\$ -0-(a)	\$ 8,275 (a)
1983	Farmers Cooperative Association Moran	293,438	45,523	-0-	187,800
1983	Kechi Elevator Kechi	94,761	42,781	81,600(a)	53,400(a)
1984	Bucyrus Grain Company, Inc. Bucyrus	297,620	30,137	-0-	157,000(b)
1984	Twombly Grain Company, Inc. Troy	760,141	730,604	2,113,091(b)	217,100(b)
1984	Englehardt Feed & Grain, Inc. Oakley	399,294	9,728	-0-(a)	33,400(a)
1985	Esbon Grain Company, Inc. Esbon	166,372	102,099	250,000(a)	99,900(a)
1985	Munkres Grain, Inc. Delevan	179,258	4,700	-0-(a)	26,000(a)

- (a) Legislative Post Audit's estimates, based on the grain shortage and amount of the warehouse's performance bond.
 (b) Grain Inspection Department estimates.

The auditors examined records at the Grain Inspection Department to try to determine reasons for these failures. They found that the records did not point clearly to any single cause. In some cases, warehouses did appear to have histories of maintaining poor financial records or having insufficient grain to cover obligations. The records for other warehouses only indicated the company did not have sufficient net worth, but the deficiencies were made up by additional bonding. Factors such as poor market conditions and possible criminal activity also contributed to some failures.



APPENDIX C
Agency Response

THE STATE OF KANSAS



JOHN CARLIN
GOVERNOR
MARVIN R. WEBB
DIRECTOR

GRAIN INSPECTION DEPARTMENT

GENERAL OFFICE

235 S. Topeka, P.O. Box 1918, Topeka, Kansas 66601

INSPECTION DIVISION

WAREHOUSE DIVISION

PHONE (913) 296-3451

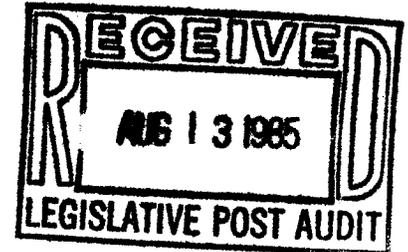
August 13, 1985

PHONE (913) 296-3454

INSPECTION POINTS

ATCHISON	KANSAS CITY
COLBY	SALINA
DODGE CITY	TOPEKA
HUTCHINSON	WICHITA

Mr. Meredith Williams
Legislative Post Auditor
Legislative Division of Post Audit
109 W. 9th Suite 301
Mills Building
Topeka, Kansas 66612



Dear Mr. Williams:

Attached is our reply to the recommendations which you sent to us on August 2, 1985. We have replied to each performance audit recommendation as clearly and concisely as possible. If you have any questions, please feel free to contact us.

We certainly are appreciative of the manner in which Mary Beth Hammerschmidt and the others worked with us on this audit. They were always very courteous and professional. We felt that they wanted to do the best job possible and do it fairly. It was a very constructive audit.

If you or anyone has any questions, please let us know. We appreciate your help.

Sincerely,

A handwritten signature in cursive script that reads "Marvin".

Marvin R. Webb
Director

MRW:csk
Attachments

RECOMMENDATIONS

(Page 16)

1. To improve its licensing procedures, the Grain Inspection Department should:
 - a. Seek legislation requiring that grain warehouses submit license applications within 90 days of the end of the warehouse's fiscal year. The Department should also be given the authority to impose fines or penalties for any warehouse's failure to satisfy this requirement.

(answer) We license grain elevators on a staggered basis each month to average the workload, i.e. with the exception of (4) months, June, July, August & December.

The average licenses per month are approximately 30 to 75.

Some fiscal closing dates are larger in some months (Dec - April) and would more or less make a few months top-heavy.

To meet the 1982 requirement, we have requested the financial statements be in our office within 90 days of the warehousemen fiscal year.

We admit that a few statements have gone beyond the 90 day limit after we have requested it, but many auditing firms have been overloaded of late and have taken more time to submit said statement.

We shall begin a ledger on all financial statements that are due, overdue and requested and what action has been taken.

We may invoke a suspension of license after a (15) day deadline for submission of said statement. I.E. the same procedure as the exception reports given by our warehouse examiners.

In conclusion, since the last post-audit of 1982, we feel we have covered the current financial statement requirement by re-evaluating the application with the new requested statement, to establish if additional bond may be needed.

- b. Analyze the financial data it receives from warehouses to evaluate the financial stability of applicants. Further, the Department should seek additional staff training or outside consultation as needed to assure that its staff has the expertise to evaluate the financial information.

(answer) Possibly budget for a C.P.A. to help review statements or on a consulting basis.

2. To improve examination procedures and ensure that those procedures are adequate for protecting grain producers, the Department should develop formal guidelines on the number of scale tickets to be tested at elevators of various sizes. The guidelines developed should provide a sample size that is manageable yet adequate for larger warehouses.

(answer) Since 1982 post-audit, we did raise the minimum scale ticket check from 10 to 20, with possibly more at the examiners discretion.

3. To help evaluate enforcement procedures, the Department should maintain a complete record of enforcement actions taken against warehouses, and the basis for each action taken. Because no such record now exists, it is difficult for the Department or the Legislature to determine if enforcement of the Public Warehouse Laws is adequate.

(answer) We will maintain & set up ledgers to record enforcement actions and the basis for such action.

APPENDIX A
(Page 23)

1982 Recommendation

1. Require that financial statements be prepared in accordance with generally accepted accounting principles.
2. Require that financial statements be accompanied by an audit or review report of a certified public accountant.
3. Require that license applications be submitted within 90 days of the date of the accompanying financial statements.
4. Develop specific tests and analyses of the financial information submitted by warehouses.
5. Review the adequacy of insurance coverage before issuing license.
6. Require that warehouses have a minimum net worth. Any difference between that minimum and the net worth of a particular warehouse would be made up through an increase in bond.
7. The Legislature should consider raising bond requirements for elevators.

Implementation

K.S.A. 34-228 amended, but Department implementation not complete.

K.S.A. 34-228 amended.

Department requests, but does not require, 90-day deadline.

Department calculates and records ratios, but does not analyze the results for licensing decisions.

Department now conducts on-site review of policy before licensing.

K.S.A. 34-228 amended.

Not implemented.

Grain Inspection Department Reply

Consider a C.P.A. Consultant on part-time basis

Much improvement.

More stringent enforcement.

We are presently on net worth requirements, but possibly a ratio of current assets to current liability could be developed. (2) States, to my knowledge have ratios as such and they are .9 to 1 - 1 to 1.

No comment

No comment

As noted, almost an impossibility and would create extreme difficulty for Kansas warehousemen to the point of forcing them out of business or applying for a Federal License whenever possible.

1982 Recommendation

Implementation

Grain Inspection Department Reply

7. Continued from page 6
8. Test the mathematical accuracy of individual settlement sheets. Implemented by Department No comment
9. Trace scale tickets to daily position records and test numerical accuracy of scale tickets. Implemented by Department No comment
10. Test accuracy of daily position records and trace daily position transactions to source documents. Implemented by Department No comment
11. Test "outbound" scale tickets as well as "inbound" tickets. Not implemented; the Department says this change is not necessary. We feel we must establish "Inbound grain" and test said "Inbound Scale tickets" because they result in all grain liabilities in the facility. Outbound is not as important, we feel, as some other items. If a problem or failure occurs, we will establish In & Out bound grain to establish a daily grain position. Grain may be moved without the use of "Outbound" tickets, i.e. RR cars or try to cover up movement.
12. Increase the number of scale tickets tested in certain areas. Department has not developed formal guidelines for sample size. On larger facilities, the examiners discretion.
13. Require examiners to document apparent violations of the Public Warehouse Laws. Implemented by Department Examiners explain to warehouseman the violation of K.S.A.

<u>1982 Recommendation</u>	<u>Implementation</u>	<u>Grain Inspection Department Reply</u>
14. Require examiners to document their follow up on prior deficiencies.	Implemented by Department	No Comment
15. Require special follow-up examinations if severe of recurring problems are noted.	List of problem warehouses maintained and those warehouses are examined more frequently	No Comment
16. Take stronger actions when appropriate.	The Department says stronger actions are being taken; auditors could not confirm.	More surveillance - examine monthly at warehouseman's expense. Increased action such as appearance before Director
17. Review complete examinations more extensively, and begin on-site evaluation of examiners.	Examinations being reviewed by central office staff in a timely manner; examiners being evaluated on-site in alternate years.	Expect to evaluate all examiners yearly.
18. Amended the Warehouse Act to provide appropriate penalties for maintaining false or duplicate records.	Amended by S.B. 300 (1985)	No comment

APPENDIX B

All (3) losses were attributable to poor market conditions and possible criminal activity.

PERFORMANCE AUDITS COMMENTS

Department was not able to provide documentation that position vacancies had been posted within the agency.

- A. All Personnel Service bulletins are posted in general office and sent to all 8 inspection stations to be posted. Enclosed are memo's sent out on notices of vacancies (Examples A)
- B. A format for interviews of applicants is being prepared for uniformity of interviewing applicants at the inspection stations. As soon as it is completed, we will forward a copy to you.

Actions related to persons who left positions appeared to be in overall compliances with State laws and regulations, but exit interview procedures could be improved.

- 1. Incumbent file could not be found.
 - a. Shirley Pipers file was misfiled and has been found. Exit interview enclosed (Example B)
- 2. File of 3 former employees did not contain exit interviews.
 - a. We don't maintain exit interviews in the employees file. They are maintained in our affirmative action file under restricted control.
- 3. Jimmy Ahrens, warehouse examiner, resigned due to health. His supervisor failed to obtain an exit interview.
- 4. Garfield Schmidt and Sean Riddle were both emergency employees and the department doesn't complete exit interviews on emergency or temporary employees, only on permanent positions. E.E.O. does not require emergency and temporary employees exit interviews when auditing an agency.
- 5. We have sent out a memo, which we copied the auditors changing the procedures on exit interviews so no supervisor would be completing them.

Some temporaries worked more than 999 hours maximum allowed for the year.

- A. A memo was put out cautioning the supervisors of their responsibilities

regarding this. We copied auditors the memo. Also, the personnel clerk was advised to over see this.

The department's use of permanently assigned vehicles was appropriated, but some vehicles are not meeting their minimum mileage requirements.

- A. The vehicles with less than the required mileage are all at the inspection stations and the one at the general office. The vehicles at the inspection stations are necessary to haul employees, grain samples and supplies to serve the grain trade. The one at the general office is used for errands to the State Office Building, etc. It has over the 80,000 miles and we are only charged for miles traveled on it. We will write Mr. Welch, General Services Director for an exemption on all vehicles located at the stations.

The department's telephone procedures were generally in compliance with state regulations, but some minor problems were noted.

- A. As stated, a policy was set and distributed to all departments in the agency. Each call is recorded by caller and checked against billing.
- B. All personal calls at the inspection stations were collected from the individuals that made them.
- C. Toll record has been kept for years, see attached memo's (Example C).

