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May 3, 1983

Letter Report P-315

Honorable Art Agnos
Chairman, and Members of the
Joint Legislative Audit Committee
State Capitol, Room 3151
Sacramento, California 95814

Dear Mr. Chairman and Members:

In response to the Supplemental Report of the Budget Act of 1982, we have reviewed the National Council on Gene Resources (council), a nonprofit research and educational organization. Our objective was to determine whether the council complied with the requirements of its contract with the Department of Food and Agriculture (department) and whether it maintained appropriate and sufficient records of its expenditure of funds for its California Gene Resources Program.

We found that the council was late in meeting almost one-fifth of the milestones in the original contract. Although the council twice submitted revisions to the milestones, the council was still not meeting almost one-fifth of the new milestones at the time of our review. In addition, the council did not obtain prior approval for 8 of 15 out-of-state trips in fiscal year 1982-83; such approval is required by the contract.

Although the council has generally maintained appropriate and sufficient records of its expenditure of funds, we found several relatively minor problems. Specifically, the council does not adequately reconcile its expenditure of nonstate funds, the council overcharged the department approximately \$700 for prepaid expenses that would benefit the council after the contract ends, and the department and the council have an expense reporting and billing system that requires unnecessary duplication of effort. Finally, there is no agreement between the council and the department for the disposition of books that the council purchased with state funds.

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The council has generally complied with the department's audit recommendations regarding the fiscal year 1981-82 contract, with the exception of three items: monthly reporting of nonstate funds, requests for purchase approvals, and review of all 1981-82 travel claims.

Because the department cancelled its contract with the council effective May 3, 1983, we make recommendations only in regard to the disposition of books purchased by the council and the financial adjustments to the council's prepaid expenses.

BACKGROUND

In 1980, the Legislature provided funds for a program to determine more effective ways for California to meet its gene resources needs. Gene resources refers to the genetic diversity needed to produce animals, plants, and micro-organisms used for society's basic needs, such as food, clothing, shelter, pharmaceuticals, and energy. Genetic diversity is needed to increase productivity, to maintain the quality of the environment, and to prevent losses in agriculture, forestry, and fishing.

On July 14, 1980, the Department of Food and Agriculture contracted with the Bodega Bay Institute of Environmental Education for 18 months of work on the California Gene Resources Program. The Bodega Bay Institute of Environmental Education was acting as the responsible contractor while the National Council on Gene Resources obtained nonprofit, tax-exempt status. Phase I of the contract, lasting 6 months, involved developing basic information on gene resources. Phase II, lasting 12 months, included the development of assessments and plans to improve research on and management of gene resources for four key commodities: strawberries, barley, Douglas fir, and salmon. This contract was funded for \$388,450.

On June 3, 1981, the contract was amended to change the official name of the responsible contractor to the National Council on Gene Resources. On June 30, 1981, this contract was further amended to extend the contract period three months and increase the contract amount to \$726,434.

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On June 30, 1982, the department entered into a contract to reimburse the council for an amount not to exceed \$633,825. Under this second contract, which is for Phase III work and covers fiscal year 1982-83, the council was to develop assessments and plans for the gene resources of two new commodities, develop proposals to establish a more effective role for the State in managing gene resources, develop plans to improve gene resources-related research, provide technical assistance for implementing existing gene resources management plans for Douglas fir and salmon, and continue an education program. The contract allowed the department or the council to cancel the contract by submitting 30-days' notice to the other party. On March 31, 1983, the department issued a cancellation notice to the council, effective May 3, 1983.

SCOPE AND METHODOLOGY

Pursuant to the Supplemental Report of the Budget Act of 1982, Item 8570-001-140, we reviewed the fiscal year 1982-83 contract between the Department of Food and Agriculture and the National Council on Gene Resources. We limited our review to the council's compliance with contract requirements and the appropriateness and sufficiency of the council's records for expenditures. Because our review took place before the contractor's final obligations were due, we compared the council's interim progress with both the milestones outlined in the contract and the revised milestones submitted by the council in September and December 1982. We also reviewed the council's compliance with other contract requirements, including the requirement that the council obtain prior approval for out-of-state travel.

We used both program and financial auditing techniques to analyze the council's contract compliance and records. We also interviewed key personnel of the council and the department, and we reviewed both financial and program files and documents relating to the California Gene Resources Program.

In reviewing financial records, we reconciled expenditures reported to the department with supporting documentation, examined internal accounting ledgers and journals, and traced expenditures to paid checks. We did not examine expenditures of previous contracts because the department had already

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audited these contracts. However, we did review the council's compliance with the recommendations made by the department's internal audit division after its review of the council's fiscal year 1981-82 records.

ANALYSIS

In the following sections, we discuss the compliance of the National Council on Gene Resources with contract provisions, the adequacy of the council's records of expenditure of state funds, and the disposition of books in the council's library. In the first section, we discuss the council's compliance with the contract milestones and the council's out-of-state travel. In the second section, we assess the council's fiscal year 1982-83 expenditure records and the council's compliance with the audit recommendations of the Department of Food and Agriculture. In the third section, we discuss the disposition of books that the council purchased with state funds.

Contract Compliance

The council has not complied with contract provisions in two areas: timely completion of contract milestones, and obtaining prior approval for out-of-state trips. The council was late in meeting contract milestones for over 19 percent of the original work activities. In September and December 1982, the council submitted new milestones to its Program Advisory Committee and to the department. The new milestones reflected the fact that early work was taking longer than originally scheduled.

We compared the work completed by the council to the revised milestones submitted in December and found that the council was still not meeting 19 percent of the milestones. The council's executive director told us early in March 1983 that he expected to complete contract requirements. It is premature to evaluate the council's overall compliance at this point; however, delays in early work may have delayed completion of the contract if it had not been cancelled.

In regard to out-of-state travel, the council did not have prior approval for 8 of 15 out-of-state trips as required by the contract and Board of Control Rule 706. The department denied approval of these 8 trips, citing inadequate justification for the trips, a Governor's Office memo

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restricting out-of-state travel to one person per trip as of October 1982, and the Governor's Executive Order freezing all out-of-state travel after January 3, 1983. Consequently, council staff used nonstate funds for the trips, saying that they could not meet contract objectives if they were not able to travel.

Adequacy of
Expenditure Records

Generally, we found that the council maintained appropriate and sufficient records of its expenditure of state funds. However, we discovered several relatively minor issues requiring attention. First, the council does not adequately reconcile its expenditure of nonstate funds. Currently, records pertaining to the expenditure of nonstate funds do not reconcile with cash balances. Reported cash balances of nonstate funds should be reconciled periodically to a detailed record of nonstate fund expenditures. Second, the council billed the department for prepaid insurance benefits and for periodical subscriptions that the council will continue to receive after both the contract cancellation date and the contract expiration date. The amount overcharged as of May 3 is approximately \$700. Third, the department and the council staff have implemented an expense reporting and billing system that requires unnecessary duplication of effort. The council submits two expenditure reports to the department each month when one report would accomplish the same objective.

Although we did not examine expenditures involved in previous contracts, we did review the council's compliance with recommendations made by the department following an audit by its internal audit division. The audit scope included a review of the council's accounting system for the 1981-82 fiscal year. The council has complied with all but three of the department's recommendations. First, the council does not include nonstate fund data on its monthly expenditure report. Second, the council does not request approval from the department for purchases over \$100. Third, the council has not reviewed all travel claims for fiscal year 1981-82.

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Disposition of Books

There is no agreement between the department and the council as to who will keep the books in the council's library after the contract ends. Since it has assumed responsibility for administering the California Gene Resources Program, the council has purchased approximately \$3,240 worth of books with state funds.

Under State Administrative Manual Section 8652, books might be classified as expendable items; therefore, they would revert to the council. However, generally accepted accounting principles state that books may be grouped into a single unit and thus classified as nonexpendable; under this classification, the books would revert to the department.

CONCLUSION

The National Council on Gene Resources was late in meeting milestones for some of its work activities. Moreover, the council did not obtain prior approval for all out-of-state trips as required by its contract with the Department of Food and Agriculture. The council has generally maintained appropriate and sufficient records of its expenditure of state funds. However, some relatively minor issues require attention. The council does not adequately reconcile its expenditure of nonstate funds, it has overcharged the department for prepaid insurance benefits and periodical subscriptions, and the expense reporting and billing system involves unnecessary duplication. Finally, the council has not yet complied with all audit recommendations, and there is no agreement regarding the disposition of books purchased by the council.

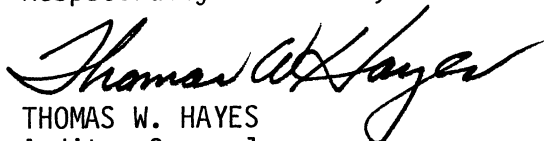
RECOMMENDATION

During the contract settlement period, the Department of Food and Agriculture should adjust the prepaid expenses for subscriptions and insurance before it makes a final financial settlement with the council. The department should also reach agreement with the National Council on Gene Resources on final disposition of the books purchased by the council with state funds.

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We conducted this audit under the authority vested in the Auditor General by Section 10500 et seq. of the California Government Code and according to generally accepted government auditing standards. We limited our review to those areas specifically contained in the audit request.

Respectfully submitted,



THOMAS W. HAYES
Auditor General

Audit Completion Date: April 25, 1983

Staff: Thomas A. Britting, Audit Manager
Margaret E. Vanderkar
Donald C. Roberts

Attachments: Responses to the Auditor General's Report
Department of Food and Agriculture
National Council on Gene Resources
Auditor General's Notes on Response from
the National Council on Gene Resources

DEPARTMENT OF FOOD AND AGRICULTURE



1220 N Street
Sacramento 95814

April 20, 1983

Mr. Thomas W. Hayes
Auditor General
660 J Street, Suite 300
Sacramento, California 95814

Dear Mr. Hayes

Members of my staff have reviewed the Auditor General's report regarding the California Gene Resources Program. This program is operated through a contract between the National Council on Gene Resources and the California Department of Food and Agriculture.

In reviewing the overall report, we recognize that the recommendations are directed only to those areas dealing with the financial adjustments concerning prepaid expenses for insurance and subscriptions, the disposition of certain items (books purchased with State funds by the Council), the inability of the contractor to meet contract compliance for completion of contract milestones, and contractor's failure to obtain prior approval for out-of-state trips.

We agree with the findings and will take those corrective actions recommended by the report. We will meet with the National Council on Gene Resources to discuss the disposition of the books that were purchased with State funds and decide whether to consider these books as a single unit and thus classify them as a nonexpendable item.

We wish to express our appreciation for the efforts of your staff in developing this report. In spite of the complexity of the issue involved in the program, your staff completed the audit expeditiously.

Sincerely

George Deukmejian
for

Clare Berryhill
Director
(916) 445-7126

RESPONSE TO LETTER REPORT P-315

A REVIEW OF THE
NATIONAL COUNCIL ON GENE RESOURCES

<u>Reference</u>			<u>Comment</u>
1. Milestones			<p>The milestones included in Contract #4302 are administrative tools subject to change. The National Council has continually reviewed its progress on contract compliance and made appropriate changes in the work plan to assure that the final reports required by the contract are produced in a timely fashion. The means (i.e., the milestones) may change but the ultimate products (i.e., the reports) and the contractually mandated time frame for completion have not changed.</p> <p>Although the most recent milestones (dated February 1983) were provided to the audit team, the comments found on page 4, paragraph 1 under the section entitled <u>Contract Compliance</u> suggest that they were not considered in the audit review. Since these milestones reflect the most up-to-date work schedule, they must be taken into consideration if an accurate evaluation is to be made.</p> <p>Since the audit was performed three months prior to the scheduled production of the contractually mandated reports, the comments found on page 4, paragraph 2 under the section entitled <u>Contract Compliance</u> are speculative in nature and not appropriate in an audit report.</p>
<u>Pg.</u>	<u>Para.</u>	<u>Lines</u>	
1	2	1-6	
4	2	1-8	
4	3	1-8	
6	3	1-2	
2. Out-of-State Travel			<p>It is the National Council's understanding that prior approval from the State for out-of-state travel is required only if the State is paying for the travel expenses. Since the State did not pay for those trips referenced in the audit report,</p>
<u>Pg.</u>	<u>Para.</u>	<u>Lines</u>	
1	2	5-8	
4	4	1-5	
5	1	1-6	
6	3	2-5	

this issue should not be part of the audit report.

3. Reconciliation of Expenditures of Nonstate Funds

<u>Pg.</u>	<u>Para.</u>	<u>Lines</u>
1	3	3-5
5	2	4-9
6	3	8-9

The National Council has had difficulty reconciling its expenditures of nonstate funds. This difficulty is a result of the timing of the State's response to requests for out-of-state travel. Several trips were initially charged to the State. However, weeks after the trips were completed the State denied the trips. Consequently, the travel expenses have to be reversed and charged to the National Council. The Council has been negotiating with the State for approval of the denied trips. As of April 1983, the National Council has been advised by the State that some of the denied trips may be paid by the State. Complete reconciliation of expenditures of nonstate funds cannot be finalized until a final decision on out-of-state travel is reached by the State.

4. Prepaid Expenses

<u>Pg.</u>	<u>Para.</u>	<u>Lines</u>
1	3	5-7
5	2	9-14
6	3	9-11

The National Council did not intentionally overcharge the State for prepaid workers' compensation insurance or technical journal subscriptions. Both areas require a 12 month prepayment rather than a month-to-month payment.

5. Expense Reporting and Billing System

<u>Pg.</u>	<u>Para.</u>	<u>Lines</u>
1	3	7-9
5	2	14-18
6	3	11-12

The National Council agrees that the State mandated expense reporting and billing system requires unnecessary duplication of effort. However, the Council has been unsuccessful in its attempts to convey this message to the California Department of Food and Agriculture.

6. Books

<u>Pg.</u>	<u>Para.</u>	<u>Lines</u>
1	3	9-11
6	1	1-6
6	2	1-6
6	3	13-15

Under the State Administrative Manual, Section 8652, books are clearly classified as expendable items. Therefore, under the terms of Contract #4302, all books belong to the National Council.

7. Compliance with
Department Audit

<u>Pg.</u>	<u>Para.</u>	<u>Lines</u>
2	1	1-5
5	3	7-11

The National Council responded to the Department's audit in December 1982. The Department has never acknowledged the Council's response nor has it ever commented on the audit.

Nevertheless, the National Council has complied with the intent of the Department's audit. For example, the Council does include nonstate fund data on its monthly report documentation sheets for Phase II, as requested by the State. The Council does request approval from the Department for all equipment purchases with a unit price of \$100 or more. The Council does not request Department approval for non-equipment items over \$100 as this was not the intent of the audit recommendation based on conversations held with the Department's auditor during the audit. Furthermore, such a recommendation for non-equipment items is not supported by prudent or common business practice. Finally, since the Department's audit included a review of all travel claims for the period referenced in their audit, the Council felt it was not necessary to duplicate their work.

AUDITOR GENERAL'S NOTES ON RESPONSE FROM THE
NATIONAL COUNCIL ON GENE RESOURCES

Reference 1. Milestones

The February 1983 milestones do not cover the period from July 1982 through January 1983; therefore, they could not be used to evaluate the early work by the council.

In the audit report, we state that delays in early work may have delayed completion of the contract. We state this because the council's later work was based on its earlier work.

Reference 2. Out-of-State Travel

As the council has recognized in its Reference No. 3, the council originally requested state payment for its trips. The council is in fact now attempting to obtain state funds for these trips.

Reference 3. Reconciliation of Expenditure of Nonstate Funds

Our report says only that records of nonstate funds should be reconciled periodically. Periodic reconciliation provides timely information on funds expended and funds remaining.

Reference 6. Books

The State Administrative Manual does not specifically address the proper property classification for books. The State Administrative Manual includes criteria pertaining to the unit cost of nonexpendable property. To apply this criteria, the council and the department must first agree on whether to consider each book as an individual unit or whether to consider books in the aggregate as one unit.

Reference 7. Compliance with Department Audit

- A. In its Phase II monthly reports, the council has not delineated state and nonstate funds. As noted in No. 3 above, the council does not periodically reconcile nonstate funds received to nonstate funds expended.
- B. The department's auditor and the council's administrator told us that previous years' travel claims had not been completely reviewed.

NATIONAL COUNCIL ON GENE RESOURCES

2855 Telegraph Avenue, Suite 209 · Berkeley, California 94705 · (415) 540-0226

April 20, 1983

Thomas W. Hayes
Auditor General
Office of the Auditor General
660 J Street, Suite 300
Sacramento, CA 95814

Dear Mr. Hayes:

Enclosed is the response to your Letter Report P-315,
a review of the National Council on Gene Resources.

Thank you for the opportunity to respond to your re-
port. It is our understanding this response will
be included in the final report.

If you wish to discuss this response, please contact
Dr. Kafton at any time.

Sincerely,



John P. Cassidy
Administrator

JPC:jh

Enclosure