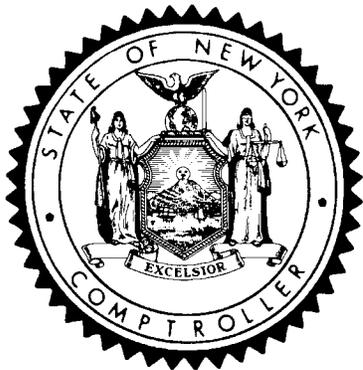


***State of New York***  
***Office of the State Comptroller***  
***Division of Management Audit***  
***and State Financial Services***

**DEPARTMENT OF AGRICULTURE  
AND MARKETS**

**ADMINISTRATION OF MARKETING  
ORDERS**

**REPORT 97-S-49**



***H. Carl McCall***  
*Comptroller*



# State of New York Office of the State Comptroller

---

---

## Division of Management Audit and State Financial Services

### Report 97-S-49

Mr. Nathan Rudgers  
Commissioner  
Department of Agriculture and Markets  
1 Winners Circle  
Albany, NY 12235

Dear Mr. Rudgers:

The following is our report addressing the Department of Agriculture and Markets' administration of marketing orders.

This audit was done pursuant to the State Comptroller's authority as set forth in Article V, Section 1 of the State Constitution, Article II, Section 8 of the State Finance Law, and Article XXV, Section 294 of the Agriculture and Markets Law. We list major contributors to this report in Appendix A.

*Office of the State Comptroller  
Division of Management Audit  
and State Financial Services*

March 31, 2000

---

---

# Executive Summary

---

---

## Department of Agriculture and Markets Administration of Marketing Orders

---

---

### Scope of Audit

The mission of the Department of Agriculture and Markets (Department) is to foster a competitive food and agriculture industry to benefit producers and consumers. In 1957, Article 25 of the Agriculture and Markets Law (Law) was enacted, authorizing the Department to make and issue marketing orders (i.e., rules and regulations) to enable agricultural producers, with the aid of the State, to more effectively correlate the marketing of their products with market demands. The Department administers four marketing orders: the Sour Cherry Marketing Order; the Apple Marketing Order; the Onion Research and Development Program; and the Apple Research and Development Program.

Under the Law, the growers must vote to approve the marketing orders and the amount of the assessment they will pay to fund the marketing orders. The Law allows the Department to contract with any organization that can provide the services required by the marketing orders. The Department has contracted with Cornell University to provide services under both the Onion and Apple Research and Development Programs. The Department also has contracted with the New York State Apple Growers Association and the New York State Sour Cherry Growers Association; these two growers associations comprise the same administrative and support staff, but have different boards of directors. The Department is to use the assessments received from the growers to reimburse the contractors for expenses that are necessary and reasonable for the execution of the marketing orders. During the 1996-97 fiscal year, more than \$1.7 million was expended to execute the four marketing orders, nearly \$1.4 million of which was for the Apple Marketing Order.

Article 25 states that the assessments collected by the Department from the growers, "shall be disbursed by the commissioner only for the necessary expenses incurred . . . with respect to each such separate marketing order . . . All such expenditures shall be audited by the state comptroller. . ."

Our mandated audit addressed the following questions relating to the Department's administration of the marketing orders for the period April 1, 1995 through June 30, 1997:

- ! Does the Department ensure that contractual services are provided and that contract expenditures are necessary and reasonable?
  - ! Does the Department have adequate revenue and accounting controls relating to the marketing orders?
-

---

## **Audit Observations and Conclusions**

We found that the Department does not determine whether the Apple Growers Association, which incurred contractual expenditures totaling nearly \$2.6 million during the two-year period ended June 30, 1997, meets its contractual performance objectives for marketing New York State-grown apples. In addition, we question whether some of the contract expenditures submitted by both growers associations to the Department for reimbursement were necessary and reasonable to fulfill the objectives of the contracts and the marketing orders. More efficient operations and better controls may result in a decrease to the amount of assessment that individual growers need to pay to support these activities.

The Department's contract with the Apple Growers Association includes marketing objectives which call for increasing the sale of New York State-grown apples by specified percentages annually in various regions of the country and abroad. However, we found that the Department does not routinely obtain sales information to assess the association's success at meeting the established contractual goals. We also observed that the Department's sour cherry marketing order, which was enacted to promote the sale of sour cherries, is in direct conflict with Federal regulations which have limited sour cherry production to control prices. Consequently, the Department's contract with the Sour Cherry Growers Association does not contain sales objectives, but primarily authorizes a few special promotional projects. The Department has used the same contractors for the marketing orders without seeking competition from other organizations which may be able to provide comparable or better services. We recommend that the Department monitor marketing order contract performance and accomplishments as required in the contract and seek additional competition for future contracts. (See pp. 7-11)

We found that controls over the Apple and Sour Cherry Growers Associations' procurement processes are poor. For example, the growers associations do not competitively select vendors to ensure they obtain the best goods and services at the best price. We also found the Department pays reimbursement vouchers submitted by the growers associations without adequate supporting documentation. As detailed in the body of this report, we question whether some of the contract expenditures incurred by the growers associations were necessary and reasonable to fulfill the objectives of the marketing orders. We recommend that the Department provide greater oversight in this area and also determine whether the questionable expenses we identified should be disallowed and refunds obtained from the growers associations. (See pp. 13-22)

---

## **Comments of Department Officials**

Department officials state that the report is inaccurate and that it does not properly present their comments related to the material presented in the report. They also disagree with most of our recommendations. The Department's complete response is included as Appendix B to this report.

---

---

---

# Contents

---

---

<b>Introduction</b>	Background . . . . .	1
	Audit Scope, Objectives, and Methodology . . . . .	3
	Response of Department Officials . . . . .	4
<b>Contract</b>	. . . . .	7
<b>Performance and Accomplishments</b>	Recommendations . . . . .	11
<b>Marketing Order Expenditures</b>	. . . . .	13
	Contract Requirements . . . . .	14
	Recommendation . . . . .	18
	Growers Associations' Expenditures . . . . .	19
	Recommendations . . . . .	22
	Department Administrative Expenditures . . . . .	23
	Recommendation . . . . .	25
<b>Department Revenue and Accounting Controls</b>	. . . . .	27
	Recommendations . . . . .	28
<b>Appendix A</b>	Major Contributors to This Report	
<b>Appendix B</b>	Comments of Department Officials	
<b>Appendix C</b>	State Comptroller's Notes	

---

---

---

# Introduction

---

---

## Background

Agriculture is one of New York State's largest industries and an important contributor to the State's economy. The mission of the New York State Department of Agriculture and Markets (Department) is to foster a competitive food and agriculture industry to benefit producers and consumers. The Department supports the economic stability of the State's agricultural industry, protects consumers from unsafe food through inspection and testing, and fosters prudent use of the State's agricultural land.

In 1957, in response to agricultural industry requests, the Legislature declared that marketing of agricultural products in excess of reasonable and normal market demand, disorderly marketing, unfair methods of competition, and the inability of individual producers to develop new and larger markets results in a waste of the State's agricultural wealth. Accordingly, it enacted Article 25 of the Agriculture and Markets Law (Law), which authorized the Department to make and issue marketing orders to enable agricultural producers, with the aid of the State, to more effectively correlate the marketing of their products with market demands. The Law was intended to establish orderly, efficient and equitable marketing of agricultural products, to reduce the economic waste in marketing the products, and to provide a means for developing new and larger markets. The Law provides that the Department's Commissioner may issue rules, called marketing orders, to regulate the processing, distribution, and handling of agricultural commodities produced and sold in New York State. Under this Law, the growers must periodically vote to continue the marketing orders and the amount of the assessment they will pay to fund the marketing orders. The Department collects assessments from the growers and enters into contracts to market the produce.

For each marketing order, the Law calls for establishing an advisory board of between five and nine members appointed by the Department's Commissioner. Nominations for these appointments are received from the commodity group for which the marketing order is established. The advisory board recommends administrative rules and regulations related to the marketing order and can recommend amending the marketing order if advisable. The advisory board also prepares and submits to the Commissioner the estimated budget required for the proper operation of the marketing order.

The Department administers marketing orders for apples, sour cherries, and onions, and works with industry to promote the sale of New York State agricultural products. This includes preparing budgets, estimating income and expenses, initiating referendums, verifying petitions, collecting assessments from growers and investigating delinquent accounts, contracting for promotion and advertising services, paying all valid claims against the orders,

---

---

and maintaining accounting and other records. The Department may use up to 5 percent of the budgeted program expenditures from each marketing order for its administrative costs and for the expenses of the advisory boards.

The Department administers the following four marketing orders:

- ! Sour Cherry Marketing Order - started in 1958 to advertise and promote new sour cherries; to conduct market and product research; and to provide related information services. Expenditures for this order for 1996-97 were \$111,738.
- ! Apple Marketing Order - started in 1959 to advertise, promote, and publicize apples and apple products; to conduct market and product research; and to provide related information services. Total expenditures for this order for 1996-97 were \$1,363,659.
- ! Onion Research and Development Program - started in 1985 to evaluate new methods to control onion maggot adults and larvae. The 1996-97 expenditures for this order totaled \$45,855.
- ! Apple Research and Development Program - started in 1990 to develop and evaluate orchard production systems that will result in increased profitability for growers. The 1996-97 expenditures for this order were \$196,200.

The Law allows the Department to contract with any organization that can provide the services required by the marketing orders. The Department must also follow the State's guidelines for awarding contracts. The Department has used the same contractors since the marketing orders were established: Cornell University to provide services under both the Onion and Apple Research and Development Programs; and the New York State Apple Growers Association and the New York State Sour Cherry Growers Association for the other two orders. These two growers associations comprise the same administrative and support staff, but have different boards of directors. Most of the direct expenses of this joint entity relate to the Apple Growers Association. Administrative and overhead expenses are shared between the two growers associations on a proportional basis.

The fruit growers and processors report and remit their assessments to the Department. The monies are deposited into a bank account and are later transferred to the Office of the State Comptroller (OSC). The Department's marketing order contracts generally provide that the contractors are reimbursed for their necessary expenses incurred in the execution of the

---

marketing orders. The contractors submit invoices to the Department, and the Department authorizes payments. The Law provides that the assessments are used to reimburse contractors for their program expenses. Under the State Finance Law, the Department is authorized to advance funds quarterly to not-for-profit contractors, such as the Apple Growers Association, to improve its cash flow and speed payment. The Department advances funds to this contractor, who is to subsequently submit vouchers to support its expenses.

Article 25 states that the assessments collected by the Department from the growers, “. . . shall be disbursed by the commissioner only for the necessary expenses incurred by the [Department] with respect to each such separate marketing order.” It further mandates that, “all such expenditures shall be audited by the state comptroller. . . .”

---

## **Audit Scope, Objectives, and Methodology**

We audited the Department’s administration of marketing orders for the period April 1, 1995 through June 30, 1997. The objectives of our audit were to determine whether the Department ensures that contract services are provided and that contract expenditures are necessary and reasonable. We also appraised the controls over assessment revenues, contract expenditures, financial accounting, and reporting for the marketing orders, and provided a statement of marketing order expenditures for the 1995-96 and 1996-97 fiscal years. To accomplish our objectives, we reviewed the Department’s financial books and records related to the marketing orders; interviewed Department officials; obtained and analyzed marketing order financial reports and records maintained by OSC; and examined applicable books and records of the organizations which the Department contracts with under its marketing order programs.

We conducted our audit in accordance with generally accepted government auditing standards. Such standards require that we plan and perform our audit to adequately assess the operations of the Department that are included in our audit scope. Further, these standards require that we understand the Department’s internal control structure and compliance with those laws, rules and regulations that are relevant to the operations included in our audit scope. An audit includes examining, on a test basis, evidence supporting transactions recorded in the accounting and operating records and applying such other auditing procedures as we consider necessary in the circumstances. An audit also includes assessing the estimates, judgments and decisions made by management. We believe that our audit provides a reasonable basis for our findings, conclusions and recommendations.

---

We use a risk-based approach when selecting activities to be audited. This approach focuses our audit efforts on those operations that have been identified through a preliminary survey as having the greatest probability for needing improvement. Consequently, by design, finite audit resources are used to identify where and how improvements can be made. Thus, little audit effort is devoted to reviewing operations that may be relatively efficient or effective. As a result, our audit reports are prepared on an “exception basis.” This report, therefore, highlights those areas needing improvement and does not address activities that may be functioning properly.

---

## **Response of Department Officials**

An initial draft copy of this report was provided to Department officials for their review and comment. The Department’s response to that draft report contained misleading and inaccurate statements, including numerous references to matters that were not contained in the draft. We considered the Department’s comments, revised our draft, shared it with Department officials, and gave the Department the opportunity to revise its response. The Department’s response to our revised draft report (Appendix B) is nearly identical to its response to our initial draft, even though we alerted Department officials to the inaccurate and misleading statements in their initial response. Department officials stated that our revised draft report was inaccurate and did not properly present their comments. They also disagreed with most of our recommendations.

We are disappointed with the Department’s response to our revised draft report, which was signed by the Department’s Director of Internal Audit, which continues to include misleading and inaccurate statements that misrepresent our observations and conclusions. The Department’s response to the revised draft report is confusing in that some of its comments relate to material that either was not in the revised draft report at all or was in the revised draft report but took cognizance of the Department’s concerns. (See Appendix C, State Comptroller’s Notes, where we address the concerns raised in the Department’s response to our revised draft report.) We disagree with the Department’s position on several aspects related to the marketing orders, especially whether they formally assess whether the specific goals and objectives included in the contract have been achieved, whether they have an effective means to monitor and control the cost-reimbursable marketing order contracts, and the reasonableness of certain growers association expenditures. Their comments to the revised draft report have been considered in preparing this final report and are included as Appendix B.

---

Within 90 days after final release of this report, as required by Section 170 of the Executive Law, the Commissioner of the Department of Agriculture and Markets shall report to the Governor, the State Comptroller, and the leaders of the Legislature and fiscal committees, advising what steps were taken to implement the recommendations contained herein, and where recommendations were not implemented, the reasons therefor.



---

---

## **Contract Performance and Accomplishments**

---

---

The Department administers and enforces the marketing orders to encourage and maintain stable prices as well as to protect consumer interests. The Department collects grower assessments and enters into contracts to conduct apple and onion research and to advertise, promote and publicize programs which will create new markets for apples and sour cherries or maintain the present markets. After a marketing order is established, it is subject to periodic referenda to determine whether the order should be continued. For example, in 1996, about 61 percent of the apple growers voted to continue the apple marketing order for an additional eight years. Between the referenda, growers may petition the Department to amend or terminate a marketing order, and the Department may suspend marketing orders for up to one growing or marketing season if the marketing order is deemed unnecessary during that season. The Department can also terminate marketing orders, subject to a referendum vote by the growers.

Department officials told us that apple marketing is aimed at developing markets and increasing sales of fresh and processed (e.g., for juice) apples; fresh apples are sold at a higher price than apples that are processed. They also told us that China will likely begin to export apples in the next decade; this could cause additional competition to New York State apple growers. The Department's contract with the Apple Growers Association includes marketing objectives which call for increasing the sale of New York State-grown apples by specified percentages annually in various regions of the country and abroad. For example, the apple marketing goals for the 1996-97 fiscal year included goals to: increase the franchise market in New Jersey, New York and Pennsylvania by 5 percent; increase the expansion markets in other states from Virginia to Maine by 5 percent; increase the national market share of New York State apples by 3 percent; increase national key buyer awareness of New York State apples by 10 percent; and maintain exports of New York State fresh apples at 10 percent of the total crop yield. The contract further indicates that the marketing plan for the expansion market in the mid-Atlantic and New England regions of the country should include advertising, in-store sampling, and point of sale materials for specific varieties of New York State apples in this market. The contract also states that the apple exports will be achieved through coordination among the Department, the U.S. Department of Agriculture, the U.S. Apple Export Council, and the International Apple Institute.

---

We found that the Department does not determine whether the Apple Growers Association, which the Department paid \$1,363,659 during the 1996-97 fiscal year, is effective in meeting its contractual performance objectives for marketing New York State-grown apples. The Department does not routinely obtain sales information to assess the Apple Growers Association's success at meeting the established goals. In addition, the Apple Growers Association does not submit required progress reports to the Department. The Apple Growers Association sends the Department an annual report, but this report does not provide sufficient information to determine whether the established goals and objectives are achieved or whether the marketing efforts have contributed to creating new markets or maintaining existing markets. Progress and sales information, including an annual Marketing Program Report, is presented at the Apple Growers Association's annual business meeting, but this data is not a performance report to the Department, nor is it in sufficient detail to assess the individual contractual objectives. For example, the contract has fresh apple sales goals for specific groups of states but the Association's report shows aggregate national sales data. Also, no data is presented regarding the contractual objectives for processed apples.

The Department's apple marketing order contract also requires the Apple Growers Association to prepare and submit either monthly or quarterly progress reports and annual progress reports which list work completed in relation to work planned, describe problems, predict the likelihood of successful program results, and estimate the economic agricultural development impact of activities and programs. The Department does not enforce this reporting requirement. The Department's Internal Auditor told us that the Department's marketing order administrator is in "routine contact" with the growers association regarding marketing order business, he attends advisory board and growers association board meetings, and that these monitoring activities far exceed what is required in the contract. He added that the Apple Growers Association prepares a biweekly publication which provides progress updates. However, this publication is a two-page trade newsletter which is intended to inform apple growers and producers about apple industry news. It does not constitute a measure of performance against contract goals and objectives.

Department records show that the State's apple producers currently sell all of their harvest, either as fresh or processed fruit. However, because fresh apples sell at a higher price than apples which are processed, there are opportunities to increase sales of fresh apples. In addition, in light of the

---

---

potential future competition from China as well as other states, New York State needs to take steps to maintain its current apple market share. Since industry conditions and needs vary from year to year, it is important for the Department to set measurable performance goals and objectives for the Apple Growers Association and to work with the association to develop strategic plans to achieve these goals and objectives and measure actual performance outcomes.

The Department's contract with the Sour Cherry Growers Association, which totaled about \$112,000 in 1996-97, does not include sales objectives; it primarily authorizes a few special promotional projects. We concluded that increased sales of sour cherries are no longer a priority of this marketing order, because the Federal government has limited the sale of New York State sour cherries to control prices. Therefore, the Department's sour cherry marketing order, which calls for taking steps to promote sour cherries and increase sales, is in direct conflict with the Federal regulations which limit sales. In addition, New York State's sour cherry industry has significantly declined in recent years; during the 1992 growing season, the 218 growers produced 31 million pounds of cherries; during the 1996 growing season there were only about 130 growers and they produced 19 million pounds of cherries. During that same period, the number of sour cherry processors also declined from seven to five.

Department statistics suggest that there is no excess capacity for New York State apples or sour cherries—all available crop harvests permitted to be sold are sold. However, there is the potential to increase the amount of fresh fruit sales. The following table, taken from Department statistical reports, shows the production and sale of apples and sour cherries for the latest five growing seasons available at the time of our audit.

New York State Grown Apples and Sour Cherries  
Sales and Production Statistics  
For the Five Growing Seasons Ended in 1996

Growing Season	Apples				Sour Cherries			
	Sales			Total Production	Sales			Total Production
	Fresh	Processed	Total		Fresh	Processed	Total	
1992	520	650	1,170	1,170	0.1	22.0	22.1	31.0
1993	400	470	870	870	0.1	15.1	15.2	15.7
1994	490	610	1,100	1,100	0.1	23.6	23.7	26.0
1995	480	630	1,110	1,110	0.2	19.8	20.0	32.0
1996	500	530	1,030	1,030	0.2	14.0	14.2	19.0

Notes:

- 1.) Quantities above are in millions of pounds.
- 2.) The Federal government limits sales of sour cherries; production above the specified limits either are left on trees or are discarded.

The Department has always had sole source contracts with the growers associations and Cornell University to provide promotional services or to do research under the marketing orders. The Department has not sought competition or requested proposals from other organizations (e.g., other agricultural research centers and advertising firms) to provide these services, and has continually awarded these contracts on a sole-source basis. Department officials stated that they are not aware of other contractors who are available and capable of providing these services. A broader distribution of request-for-proposals may identify additional entities capable of performing this work.

---

## **Recommendations**

1. Establish a formal reporting structure to directly measure performance against the contracted goals and objectives for the marketing orders to determine whether the desired results are achieved. Consider entering into performance-based contracts that match payments with the achievement of contract goals and objectives.

(Department officials disagree with this recommendation and assert that measurable goals and objectives are already established and monitored. They did not respond to our recommendation to consider performance-based contracts in the future. Although the Department's contracts with the Apple Growers Association included performance goals, we found there was no formal reporting to the Department of actual performance against those goals.)

2. Seek competition for future marketing order contracts, such as from other agricultural research organizations and advertising agencies.

(Department officials disagree with this recommendation and state that they use sole source contractors and the Department is not aware of other contractors available and capable of providing such services. We strongly encourage the Department to seek competitive proposals from other agricultural research organizations, as well as from advertising agencies, when the current marketing order contracts expire, to formally determine whether other entities can provide better and/or less-costly services.)

---

# Marketing Order Expenditures

We audited the expenses made from the State accounts related to the four marketing orders for fiscal years 1995-96 and 1996-97. The primary expenses charged to the accounts represented contract payments. As previously discussed, the Department has contracts with Cornell University to administer grants for the Onion and Apple Research and Development Programs, and with the New York State Apple Growers Association and the New York State Sour Cherry Growers Association to administer the apple and sour cherry marketing orders. The market order expenses also include the reimbursement of the Department's administrative costs. The following table represents the expenses of the four marketing orders which were charged to the State accounts.

Department of Agriculture and Markets Marketing Orders Comparative Statements of Expenditures 1996-97 and 1995-96 Fiscal Years								
	Apple Marketing Order		Sour Cherry Marketing Order		Apple Research and Development Program		Onion Research and Development Program	
	1996-97	1995-96	1996-97	1995-96	1996-97	1995-96	1996-97	1995-96
Agriculture and Markets Expenditures	\$42,681	\$44,349	\$4,738	\$5,047	\$7,980	\$12,467	\$1,975	\$1,839
Contracts/Grants	1,320,978	1,180,436	107,000	109,000	188,220	162,823	43,880	40,638
Total Expenditures	\$1,363,659	\$1,224,785	\$111,738	\$114,047	\$196,200	\$175,290	\$45,855	\$42,477

Notes:

- 1.) Expenditures are presented under the modified accrual basis of accounting.
- 2.) The Apple Marketing Order, the Sour Cherry Marketing Order, and the Apple Research and Development Program fiscal years end June 30; the Onion Research and Development Program fiscal year ends March 31.

We evaluated controls and practices of Cornell University's Office of Sponsored Funds, which coordinates the market order-sponsored apple and onion research projects. We concluded that Cornell University is well positioned to administer these research programs: there is a strong control environment; appropriate records to support financial transactions; information systems to produce operational, financial, and compliance-related reports; and an effective performance monitoring system. Cornell University administers a large number and dollar value of research grants and has a system in place to administer grants in compliance with various State and Federal regulations.

---

We also evaluated controls and practices at the growers associations and found poor administrative controls and question whether some of the expenditures submitted by the growers associations to the Department for reimbursement were necessary and reasonable to fulfill the objectives of the marketing orders. The Department does not have an effective process to ensure that the growers money is prudently, appropriately and reasonably spent to accomplish marketing order goals and objectives.

---

## **Contract Requirements**

The Department's contracts with the Apple and the Sour Cherry Growers Associations are generally not specific as to which types of expenditures are allowable. Instead, they state that each reimbursement voucher should detail expenditures and that reimbursement can be withheld if all required progress reports are not received. Department officials told us that the growers associations are not State operations and are not financed with taxpayer funds; the marketing order assessments represent the Department's collection of the growers' money which they have collectively agreed to pay for expenses related to the marketing orders. Further, they believe that since the growers associations' boards of directors represent the growers, it is up to these boards to ensure that the growers associations spend the grower assessments properly toward achieving the goals and objectives of the marketing orders. However, legislation requires the Department to collect the assessments and to only pay for necessary program expenses incurred with respect to the marketing orders. The Department clearly has a fiduciary responsibility to the growers for prudently administering the market orders. In addition, the Department has responsibilities under its contracts with the Apple and Sour Cherry Growers Associations to ensure that expenses are reasonable and necessary to fulfill the program goals stated in the contracts.

We found that the Department needs to strengthen and enforce the language in its contracts, especially with regard to the use of program expenditures. Following are some areas in which the contract provisions are not enforced or that additional contract requirements are needed to improve controls.

**Subcontracts** - Although the marketing order contractors are required to have formal subcontract agreements which clearly describe the goods and services provided, we found that the growers associations routinely acquire goods and services without entering into formal subcontracts. For example, the growers associations use outside consultants to assist with out-of-state promotional activities and pay these consultants a monthly fee plus travel and other direct expenses. However, there are no formal contracts with the

---

consultants for these services and, accordingly, no documentation of what services are to be provided and how much it will cost.

The Department also does not require the growers associations to competitively select vendors to ensure that they obtain the best goods and services at the best prices. We also noted instances where the growers associations conducted business with out-of-state companies without competitive bidding. According to officials of the growers associations, it is less costly to deal with these companies. However, without competition, they have no assurance that this is true. The Department should ensure that bidding requirements are part of its contracts with the growers associations, thereby ensuring the best prices are obtained and enabling other businesses, including New York State businesses, the opportunity to compete.

**Expenditure Documentation** - The Department's Marketing Order Manual states that the Department's marketing order administrator must review paid invoices before approving payment vouchers to the contractors; but we found that documentation is not requested or submitted. Department officials told us that they had previously required the growers associations to submit copies of paid invoices with their reimbursement vouchers; however, the Department currently does not require supporting documentation. Instead, the Department requires the growers associations to submit vouchers which list the name of the payee, the expense category, and the amount of the expense. We found that the Department's review of these vouchers is cursory at best. The Department's Internal Auditor stated that there is no need to require voluminous documentation from its marketing order contractors because the growers associations are regularly audited by OSC, as well as a public accounting firm. The Department has a fiduciary responsibility to disburse funds only for the necessary expenses incurred with respect to each market order. Department officials should not rely on OSC's post audit to meet their internal responsibility.

The contracts require the growers associations to establish and maintain complete and accurate books, records, documents, accounts, and other evidence directly pertinent to performance under the contracts. We visited the growers associations and examined their books and records. We found the growers associations conduct business in a very informal manner. Purchasing records at the growers associations are often incomplete and in some instances do not exist. There is limited supporting documentation for expenditures. For example, there are generally no receiving reports for purchases made from vendors, we could not always determine the purpose of travel and other travel-related expenditures, and there is generally little, if any, documentation to support whether goods and services are provided

---

satisfactorily. The lack of adequate documentation prevented us from further analysis to determine whether goods and services have actually been received.

The Department's Internal Auditor indicates that check numbers, dates, payees, and amounts on reimbursement vouchers are sufficient information to allow the Department to fulfill its responsibility to the growers that their money has been spent appropriately. We do not believe this is sufficient. For example, the growers associations routinely use credit cards for purchases and only list on the vouchers submitted to the Department the name of the credit card company as the payee, without any further detail as to the nature of the expenses. For the two years ended June 30, 1997, the growers associations submitted to the Department more than \$100,000 in such credit card expenses. Under these circumstances, the Department is not aware of the detail of these expenses. (Based on our review of these transactions, we questioned a number of expenses which were charged to credit cards, and we present examples of such expenses later in this report.)

In addition, we noted that information on the reimbursement vouchers does not always match the growers associations' records. For example, we found that the check numbers for some growers association expenses are different from what has been reported to the Department. We also observed situations where the growers association made installment payments to vendors for building renovations and office furniture, yet claimed full reimbursement at one time.

We maintain that the Department is primarily responsible for administering the market order contracts. The Department needs to exercise fiscal oversight and closely monitor marketing order expenditures. If Department officials decide not to routinely require additional expense documentation, we urge them to periodically validate the propriety of expenses which the growers associations include on their reimbursement vouchers through field reviews (e.g., using sampling techniques).

**Expenditure Guidelines** - Although Department officials have set criteria for reimbursing contract travel expenditures (i.e., they limit travel expenses to the prevailing State rates), we found they do not enforce them. For example, we noted where the Department reimbursed the associations for hotel accommodations which exceeded the maximum allowable rates, and paid for the cost of meals in excess of allowable amounts. They allowed travel expenses which included liquor, movies and laundry services. Further, several of these expenses were incurred for the Apple Growers Association's executive staff and for members of its board of directors, without evidence

---

that they were business-related expenses. The Department's Internal Auditor informed us that, as a result of our audit, the Department now requires the growers associations to document the need to exceed allowable per diem travel rates. However, the Department needs to also establish guidelines for other than travel expenses. The contract only states that expenses be used to promote, advertise and publicize New York State apples and apple products. Additionally, there are no guidelines requiring advance approval for expenses in excess of designated dollar amounts. Such guidelines need to be established.

**Internal Control Weaknesses** - The Apple and Sour Cherry Growers Associations have very weak internal controls; for example, the executive director is also the assistant treasurer. This results in incompatible duties as the assistant treasurer signs checks which the same person, as executive director, authorizes. Therefore, there is no independent review over this payment process. Growers association disbursement checks require two signatures, but the other authorized signatory is the accounting clerk, who maintains the accounting records and, as such, should not sign checks. The accounting clerk also reconciles the growers associations' bank accounts. We also found that a stamp with the assistant treasurer's signature is used to sign checks in his absence.

As noted above, both of the individuals who sign the growers associations' checks have incompatible duties which should preclude them from signing disbursement checks, and there are no other controls to compensate for this internal control weakness. However, the Department's Internal Auditor considers it inappropriate to "micro-manage" the business of contractors. We believe internal controls are important. There is a higher likelihood of fraud and abuse, of which the Department should be concerned, where there are weak internal controls. The Department is essentially the sole source of finances to the growers associations; we think it is even more important to ensure that controls are adequate because virtually all of the growers associations' activities are concerned with the marketing orders. We strongly urge the Department to work with the growers associations' governing boards to institute appropriate internal controls. Without adequate control at the growers associations, the Department cannot have adequate assurance that business is conducted properly, contract requirements are properly fulfilled, and that the potential for fraud and abuse is reduced. While we acknowledge that the growers associations have limited staff with which to fully separate duties and provide an ideal internal control environment, there should be minimal separation of duties and compensating controls, such as having an independent bank reconciliation and providing supervisory review and oversight. The Department's Internal Auditor told

---

us that he has forwarded our comments regarding internal controls to the growers associations.

### **Recommendation**

3. Strengthen and enforce provisions of the marketing order contracts with the New York State Apple Growers Association and the New York State Sour Cherry Growers Association by requiring them to:
- ! maintain complete and accurate books, records, documents, and accounts;
  - ! enter into formal contracts for purchasing goods and services;
  - ! seek competition for purchases, giving New York State businesses a chance to bid on growers association purchases;
  - ! periodically submit supporting documentation with selected vouchers;
  - ! adhere to comprehensive expenditure criteria, which the Department should establish; and
  - ! establish satisfactory internal controls, including separation of duties in the executive director/assistant treasurer's function and limiting the practice of signing checks with signature stamps.

(Department officials agree to require that the growers associations enter into formal contracts for major purchases of goods and services. However, they state that the growers associations already maintain accurate books and records, solicit competition for major purchases, submit adequate documentation for pre-audit purposes, and have adequate expenditure criteria and internal controls. Our audit found no indication that the growers

---

### **Recommendation (Cont'd)**

associations competitively bid major purchases. Also, as noted in the body of this report, we found the growers associations' reimbursement vouchers were sometimes inaccurate and did not provide sufficient detail for Department oversight. Additionally, the marketing order contracts only include expenditure criteria for travel expenses and we identified internal control weaknesses during our audit at the growers associations.)

---

## **Growers Associations' Expenditures**

The Department's marketing order contracts generally provide that the contractors are reimbursed for their necessary expenses incurred in the execution of the marketing orders. The contractors submit invoices to the Department, and the Department authorizes payments. The Law provides that the assessments are used to reimburse contractors for their program expenses.

We selected a judgmental sample of expenses at the growers associations which included high dollar items, expenses paid to selected vendors and individuals, and travel expenses. Based on our review of supporting documentation, we found that the growers associations have claimed, and the Department has paid, some expenses which we believe are questionable as reimbursable—they were either not documented, they were costly, or they may not have been necessary and prudent to promote the purpose of the marketing orders. Following are some examples of growers associations' expenses which we questioned and should be fully investigated by Department program and audit staff:

- ! The growers associations have assigned credit cards to three of their staff. The three individuals using these credit cards had more than \$100,000 in credit card purchases in a two-year period. For many of these purchases, the only documentation for the expense was a copy of the credit card charge slip, and these charges were generally not formally authorized in advance. Examples of expenses which were on the growers associations' credit card bills, the details of which were not provided on the vouchers which the Department paid, include:

---

S expenses for which there were either no supporting documentation or were not explained on expense reports (\$9,364),

S expenses which appeared excessive or inappropriate (\$3,542),

S meals for the spouses of board members/staff,

S meals at restaurants located near the growers associations' office for staff and holiday luncheons (\$1,668), and

S rental charges for vans to transport board members and staff from board meetings to restaurants (\$1,000).

- ! Within a year and a half, the growers associations purchased three vehicles (two sports utility vehicles and one minivan) at an average cost of nearly \$30,000. The growers associations purchased these vehicles from a nearby automobile dealer; there was no documentation to support that competition was sought for such large purchases. The cost of these vehicles exceeded the amounts approved by the growers associations' boards of directors. Also, there are no prohibitions against personal use of these vehicles (the employees are to reimburse the associations for personal use at a rate of \$.06 per mile). Based on our review of job descriptions, it appears that at least one of these vehicles should not have been purchased, since travel is generally not required of the individual assigned the vehicle. In addition, based on our review of how these vehicles were used, the growers associations should have been able to function by purchasing one vehicle and reimbursing employees for business use of their personal vehicle. The Department's Internal Auditor stated that these vehicles were part of individual employee compensation packages.
  
- ! The Department reimbursed the growers associations for travel expenses which were in excess of the prevailing State rates. This occurred because the Department did not have an adequate system in place to review and approve travel expenses. For example, the growers associations did not submit supporting documentation or expense reports with their reimbursement vouchers. In addition, they incur travel expenses in a combination of ways—using both credit cards and expense vouchers. These conditions do not enable the Department to properly monitor travel expenses. The Department even reimbursed the growers associations' cost of laundry service and in-room movies while their staff or board members travel; in some instances three or more movies were ordered in a single evening. In addition, we noted where the

---

Apple Growers Association paid travel expenses (\$1,686) relating to business activities for the Sour Cherry Growers Association.

- ! The growers associations spend significant amounts of money on airfare. The president of the growers associations has joined various airline travel clubs at the growers' expense to conduct "routine business during airport layovers." There was only documentation for three such meetings during the two years we audited. Our review of travel expenses disclosed that the Apple Growers Association also paid the airfare for a spouse to attend a trade show.
- ! The Department generally does not question expenses which the growers associations have coded as "general expenditures," even though we found payments for parking tickets, alcohol, candy and gifts which were coded as general expenditures.
- ! The growers associations claimed and were paid for at least one expense twice.

The Department's Internal Auditor stated that the growers associations are not government operations financed with taxpayer dollars, but are businesses having boards of directors elected by the growers. Accordingly, some expenditures which would not be allowable for a government entity may be valid and expected from a marketing organization (e.g., entertainment expenses). Although the growers associations are not governmental agencies, they are not-for-profit corporations that have entered into contractual agreements with the Department. The Department has a fiduciary responsibility to ensure that costs claimed by the associations are allowable, documented, and incurred for services funded under the contractual agreements.

The Department's Internal Auditor added that the best assessment of program effectiveness may be that a majority of growers had voted to continue the marketing orders. He also indicated that he believes most of the examples cited above are legitimate expenses and they are not material. We present these examples in conjunction with the growers associations' weak internal controls and minimal Department oversight to raise the Department's concern. More efficient operations and better controls may result in a decrease to the amount of resources that growers need to submit to support these activities.

---

## **Recommendations**

4. Investigate whether the expenses which we questioned in this report should be disallowed and the amounts paid recovered from the growers associations.

(Department officials agree with this recommendation.)

5. Improve monitoring of the growers association contracts by:

- ! periodically requiring the growers associations to submit supporting documentation with selected vouchers;
- ! consistently monitoring and reviewing vouchers submitted for reimbursement to determine whether expenses claimed are reasonable, and are for the intended purposes of the marketing orders;
- ! having program or fiscal staff periodically review payment documentation at the growers associations; and
- ! requiring Department review and prior approval for large expenses.

(Department officials disagree with this recommendation and state that they properly review contractor performance. As we note in the body of this report, the Department relies on summary information provided by the growers associations which only indicates the payment amounts, dates, and payees. This information is not sufficient for the Department to properly oversee the contracts. For example, numerous expenses are included in the growers associations' credit card charges, which are supported only by a credit card slip. Also, considering the nature of some of the expenditures we present in the report, we believe it is appropriate for the Department to exercise its fiduciary responsibility to the growers by requiring advance approval of large purchases and periodically reviewing the reasonableness of other selected expenses.)

## Department Administrative Expenditures

The Law authorizes the Department to withhold up to 5 percent of the monies collected from each marketing order to defray its costs to administer the orders. The Department's rules and regulations further define this process: the total amount of administrative costs should not exceed 5 percent of the total budget. We found that the Department does not closely monitor the amount of administrative expenses it charges to the marketing orders to ensure it complies with the Law. We also found that the Department does not have a good cost accounting system to accumulate all Department costs related to each marketing order. As a result, the Department undercharged its administrative expense to some marketing orders and overcharged others.

A summary of the revenues collected by the Department and the Department's administrative expenses charged to the various marketing orders for the 1995-96 and 1996-97 fiscal years is shown in the following table:

Department of Agriculture and Markets Marketing Orders Summary of Revenues Collected and Administrative Expenses 1996-97 and 1995-96 Fiscal Years								
	Apple Marketing Order		Sour Cherry Marketing Order		Apple Research		Onion Research	
	1996-97	1995-96	1996-97	1995-96	1996-97	1995-96	1996-97	1995-96
Total Budget	\$1,844,000	\$1,062,500	\$149,500	\$166,900	\$279,000	\$220,626	\$67,950	\$67,700
Budgeted Administrative Assessment	\$69,149	\$81,633	\$5,273	\$4,990	\$9,213	\$8,555	\$2,000	\$2,000
Maximum Allowable Administrative Assessment (5 percent)	\$92,200	\$53,125	\$7,475	\$8,345	\$13,950	\$11,031	\$3,398	\$3,385
Administrative Expense Charged	42,681	44,349	4,738	5,047	7,980	12,467	1,975	1,839
Under (Over) Charged	\$49,519	\$8,776	\$2,737	\$3,298	\$5,970	(\$1,436)	\$1,423	\$1,546
<p><u>Notes:</u> 1.) Department officials state that \$1,500 was paid to Cornell University during 1995-96 to publish research results and was not an administrative charge for Apple Research that year; accordingly the Apple Research administrative expenses were not overcharged by \$1,436 during 1995-96, but were undercharged by \$64. However, the Department did not provide us with documentation for this expense.</p> <p>2.) Net Amount Undercharged for the Two Fiscal Years = \$71,833 (or \$73,333 total undercharged after applying the \$1,500 payment to Cornell University).</p>								



---

The above table shows administrative fees budgeted, the maximum administrative fees that could be charged (at 5 percent of the total operating budget), and the amount that was actually charged to the marketing orders. The Department undercharged its administrative costs. In the aggregate, the Department could have charged more than \$70,000 in additional administrative costs to the marketing orders for the two fiscal years. We noted that there were surplus marketing order funds in the Department's custodial account during this period.

The Department estimates its indirect administrative costs as well as the amount of time staff directly spend on marketing order activities and charges the growers' assessments for the dollar value of this time. However, we found that the Department did not charge payroll costs for the Marketing Order Administrator or the Director of Agriculture Protection and Development Services, both of whom spend time on marketing order activities. Some costs of these two Department officials are charged to marketing order administrative costs as a general overhead charge, which is less than if these individuals' marketing order efforts were charged as a direct cost. The marketing orders should pay these State expenses to the extent that these additional salaries and fringe benefit costs are attributable to marketing orders, but are less than the maximum allowable administrative fee. Otherwise, State taxpayers are unnecessarily paying costs which the marketing orders were intended to reimburse.

The Department's Internal Auditor maintains that the Department has discretion regarding the amount of administrative costs it charges to the marketing orders, and Department officials prefer that the funds be spent in other areas. However, he added that Department resources are used to promote a wide variety of other agricultural commodities which are not covered by marketing orders.

We believe the Department should maximize reimbursement of its applicable marketing order administrative expenses. If the Department charged more allowable administrative costs to the marketing orders financed by the grower assessments, it would have more State funds available to promote other agricultural products.

---

### **Recommendation**

6. Charge to the marketing orders for all Department administrative employees who work on the marketing orders.

(Department officials disagree with this recommendation and state that they do not have to charge the marketing orders for administrative employees who work on the orders. We agree. However, to maximize reimbursement of State costs attributable to the marketing orders, the Department should charge the full cost attributable to marketing orders for all of the administrative employees who work on the marketing orders, rather than allocating only some of their costs.)



---

---

## Department Revenue and Accounting Controls

---

---

Fruit growers and processors covered by the marketing orders submit production reports to the Department. These production reports are the basis of the marketing order assessments and serve as the Department's tool for program budgeting purposes. The Department validates the mathematical accuracy of the amounts due based on reported production totals. However, other than desk reviews, it does not verify the accuracy of the information which growers report. Department officials informed us that they are aware that not all of the required fruit growers and processors pay the marketing order assessments. In addition, they have recently begun the process of purchasing outside audit services to conduct post audits of grower and processor production reports.

Effective internal control includes a segregation between the preparation of bills and invoices, the receipt of cash related to these bills and invoices, and the associated record keeping. This includes periodic independent reconciliations between cash receipts and the accounting records. We found a serious weakness in these controls because the Department staff person who maintains the accounting records for the marketing orders also prepares bills to growers, receives assessment checks and reconciles the marketing order accounting records to the Department's Finance Office records.

The Department prepares financial reports for each of the marketing orders. However, these reports are not in full conformance with generally accepted accounting principles. For example, although the Department prepares statements of revenue and expenditures and a balance sheet, it does not prepare a statement of changes in fund balances. The Department's Internal Auditor stated that the statements are in compliance and the statement of changes in fund balance is not necessary or required. However, all three statements are required according to generally accepted accounting principles. In addition, the Department records its accounts payable on the date that its staff approves contractor invoices, not when the expenses were incurred, as required under generally accepted accounting principles.

---

## **Recommendations**

7. Separate the duties of billing, collection and record keeping.

(Department officials disagree with this recommendation because they believe the cost of separating duties would exceed expected benefits. We believe the Department should be able to implement these basic internal controls at minimal expense using existing staff, possibly from other Department divisions. At a minimum, the Department should assign an independent person the responsibility for processing the receipt of grower assessments and an independent person the responsibility for reconciling the financial and accounting records. Given the internal control weaknesses we identified, the Department should also ensure that there is adequate supervision and oversight over marketing order financial activity.)

8. Prepare complete financial reports in conformance with generally accepted accounting principles.

(Department officials disagree with this recommendation and assert that marketing order balance sheets and income statements are prepared in conformance with generally accepted accounting principles. We found, however, that the Department does not prepare a statement of changes in fund balance, a requirement of generally accepted accounting principles.)

---

---

# Major Contributors to This Report

---

---

Frank J. Houston  
Walter Mendelson  
Roger Mazula  
Charles Krahula  
Kenneth Cox  
Judy Middelkoop  
Deb Spaulding  
Paul Bachman



STATE OF NEW YORK  
DEPARTMENT OF AGRICULTURE AND MARKETS  
1 WINNERS CIRCLE  
ALBANY, NEW YORK 12235

DIVISION OF INTERNAL AUDIT  
518-457-2771

July 23, 1999

Mr. Frank Houston  
Audit Director  
Office of the State Comptroller  
Division of Management Audit  
270 Broadway, 19th floor  
New York, NY 10007

Dear Mr. Houston:

Attached is the Department's response to the Comptroller's draft audit report of the Department's administration of market orders.

The Department of Agriculture and Markets always welcomes audits which provide an independent, objective and thorough review of our programs; and willingly accepts recommendations which improve the efficiency and effectiveness of operations. We believe this report, however, does not meet these objectives. After spending thousands of hours over the past four years on audits of the Department's administration of market orders it is extremely discouraging to receive a report that contains misstatements of fact, faulty observations, erroneous conclusions and impractical recommendations. Despite four years of numerous discussions, meetings and written correspondence with various auditors, during which we received many different versions of preliminary and draft reports, this latest version, in our view, still does not present an objective and unbiased appraisal of market order operations and the Department's role in administering them.

As noted in discussions and comments on previous drafts, the Department continues to be concerned that our responses to previous versions of the report have generally been inaccurately presented since many statements attributed to Department officials were not made in the context presented. We expect that the final report will include our response in its entirety so that our comments are presented fairly and accurately.

\*  
Note  
1

\*  
Note  
2

printed on recycled paper

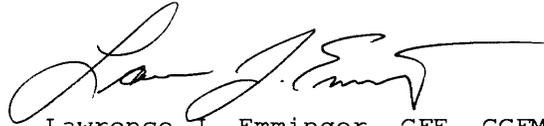
\*See State Comptroller's Notes, Appendix C

**Appendix B**

While previous efforts by the Department to correct report inaccuracies have been unsuccessful, we continue to hope that you will correct them prior to finalizing.

If you have any questions regarding the Department's response, please contact me.

Sincerely,



Lawrence J. Emminger, CFE, CGFM  
Director of Internal Audit

attachment

---

**DEPARTMENT OF AGRICULTURE AND MARKETS  
RESPONSE TO DRAFT AUDIT REPORT #97-S-49**

**TRANSMITTAL LETTER**

The Commissioner's name is spelled Davidsen.

**EXECUTIVE SUMMARY**

The Executive Summary presents an incomplete, inaccurate and distorted assessment of market order operations in New York State. The summary fails to recognize the significant achievements of each order since their inception. Internationally recognized research results are ignored in the report as are the economic benefits achieved by New York growers as a result of the orders. For example, there is no mention in the report that sour cherry growers received 157 percent more per pound for their crop in 1998 as compared to 1997.

\*  
Note  
3

The report's conclusion that the Department is not effective in measuring contract performance is erroneous since it ignores oversight efforts by the Department, Market Order Advisory Boards and the Apple and Sour Cherry Growers Association Boards. Evaluation of performance against contract objectives is continuously monitored throughout each contract year with a comprehensive and formal evaluation at year end. While documentation of this year end assessment was provided the audit team it has for some reason been ignored.

\*  
Note  
4

The executive summary also erroneously states that the Federal and State sour cherry orders are in direct conflict with each other. Previous versions of the report contained a recommendation that the State order be discontinued, and while this version does not, the inference remains. Such statements reflect the lack of even the most basic understanding of market orders and the purpose they serve.

\*  
Note  
5

The report presents no credible evidence that expenditures incurred by the grower associations under their respective contracts were unnecessary and

\*  
Note  
6

---

\*See State Comptroller's Notes, Appendix C

unreasonable. Citing several travel related expenses inadvertently paid in error over a two year period as the basis for such a blanket statement is at best an exaggeration. Other expenses questioned in the report have no basis in fact. The statement that the Associations did not obtain competitive bids on certain items is also incorrect. While the documentation the audit team seemed to be looking for was not as formal as they would have liked, this does not mean that bids were not solicited.

\*  
Note  
7

Documentation submitted by the Associations to support contract expenses is sufficient. To require the Associations to submit copies of payrolls, invoices and canceled checks with each reimbursement voucher is impractical for obvious reasons. Also ignored is the fact that the Department contracts with approximately 200 external entities. If we require such extensive documentation for one we would need to require it from everyone.

\*  
Note  
8

The Department has strictly adhered to the Comptroller's guidelines for awarding contracts to Cornell University and the New York Apple and Sour Cherry Grower Associations. Annual approvals of their sole source status are obtained from your Office. Notices of intent to award these sole source contracts are published in the State Contract Reporter so even if there were other organizations available they would have the opportunity to submit proposals.

**Introduction**

**Background**

There are several topics that we believe should have been addressed in the background section so as to present a more complete and objective explanation of market order operations. This section focuses on the administrative responsibilities of the Department with little mention of what growers are trying to accomplish through establishment of the orders. It needs to be highlighted that it is the growers that initiate Orders. The New York Apple

---

\*See State Comptroller's Notes, Appendix C

Association and its predecessor organizations were around long before creation of the Apple Marketing Order(AMO) in 1959 and were the driving force behind the establishment of the order. The order did not create the Apple Growers Association that was in place at the time.

The Sour Cherry Order is not limited to advertising and promotional activities as the report incorrectly states. Market and product research and informational services are permitted under the order.

\*  
Note  
9

Contractors under the market orders are not-for-profits (NFP's) entitled to the protections afforded by Article 11-B of the State Finance Law. The Comptroller's regulations implementing this law require us to issue written directives allowing advance payments for any renewal contracts. We have also written advances into the contracts themselves, in keeping with contractor needs and with the intent of the law and regulations to speed payments to NFP's.

**Contract Performance and Accomplishments**

The statement that the Department does not determine whether the New York Apple Association is effective in meeting its performance objectives is not supported by the available documentation. Statements attributed to the Marketing Order Administrator regarding established goals are not accurately presented in the report and we would like them either corrected or removed. This is one of many instances where Department officials' comments have been selectively omitted, misstated or misrepresented in the report.

\*  
Note  
10

While the report makes a detailed presentation of the 1996-97 marketing year objectives for the Apple Marketing Order, there is no reference to the year end Marketing Program Report presented at the NYAA Board meeting in July, 1997. This Program Report, which was provided to the audit team, presents a detailed analysis of how the year's marketing objectives were achieved and assesses performance against the contractual objectives. There is also public and proprietary apple marketing data available at the NYAA that, to our knowledge, was never reviewed by the audit team.

\*  
Note  
11

---

\*See State Comptroller's Notes, Appendix C

The Apple Marketing Order Administrator, Apple Marketing Order Advisory Board and the New York Apple Association Board of Directors are all involved in approving and monitoring performance objectives throughout the year. This is not just an end of the year process. It is our conviction that our contract monitoring activities far exceed those required in the contract. While the contract only requires quarterly reports, the Department is in routine contact with NYAA staff members and members of the Advisory Board. Department officials receive a bi-weekly publication from the NYAA detailing what activities are going on. The Marketing Order Administrator attends both Advisory Board and NYAA Board meetings during which detailed presentations are made and discussions held regarding performance against contractual objectives. All of these forums meet the intent of the quarterly report referenced in the contract and in reality exceed the usefulness that such a report would provide. We also disagree with the report's remarks about the effectiveness of the bi-weekly "Core Report" as one of many tools used to monitor program effectiveness. This report is sent to a variety of people involved in the apple industry including growers, packers, processors, retailers and Department officials. Not only does it contain much of the same information contained in a quarterly report but it does so in a more detailed and timely manner.

Comments made on page seven present a simplistic and misleading description of apple and sour cherry marketing in New York. To state that there is no excess capacity of apples and sour cherries and that all available crop harvests are sold as the basis for implying that marketing orders are no longer needed reflects a lack of even the most basic understanding of market dynamics. To say that Department statistics suggest this is even more incredible. Yes, a grower may eventually sell all of his/her apples, but apples sold for processing in June generate only a fraction of the income the grower could have gotten if sold the preceding October or November as fresh.

* Note 12
-----------------

---

*See State Comptroller's Notes, Appendix C
--

**Recommendations**

1.) Disagree. Measurable goals and objectives are already established and monitored. The report's statements to the contrary are inaccurate and not supported by any facts.

2.) Disagree. Cornell University and the New York Apple and Sour Cherry Associations are sole source contractors. The Department is aware of no other contractors available and capable of providing services.

**Marketing Order Expenditures**

The Department disagrees with the conclusions drawn in this section of the report since they are based on erroneous assumptions and misstatements of fact. The Department maintains a very good cost accounting system for the Marketing Orders to both account for revenues and monitor expenses. At any given point in time the exact financial position of an order can be determined. A balance sheet and income statement prepared in conformance with generally accepted accounting principles is provided to Department managers and Advisory Board members on a monthly basis. This accounting system was developed in part because the State's Centralized Accounting System, which your Office maintains, did not provide timely or useful information with which to administer the orders effectively.

Contrary to the report's contention, the Department has an effective system in place to monitor contractor performance and ensure grower money is spent appropriately. The Department requires the New York Apple and Sour Cherry Associations to submit more documentation than Cornell University when requesting payments under the contracts. We do not understand why the information Cornell submits is deemed satisfactory while what the Associations submit is not. The Department requires that each Association's voucher be accompanied by a list itemizing each expenditure including payee, check number, date and amount. The Department reviews the vouchers and supporting

documentation and, when warranted, questions certain expenditures. While the report recommends we require this extensive documentation for the Associations it ignores the fact that at any given time the Department administers up to 200 contracts. To require payrolls, invoices and canceled checks for each item of expense claimed for each of these contracts would not only be impractical, unreasonable and extremely expensive, it would provide us with no greater level of assurance that funds were properly expended than we have now. If we require such extensive documentation for one contract we will need to require it for all. In the case of the Associations, both are regularly audited by a public accounting firm. Finally, since your Office is required to conduct an annual audit, there is no need for us to require such voluminous documentation or conduct duplicative audits on our own.

\*  
Note  
8

**Contract Requirements**

This section of the report again takes selective portions of discussions with the audit team and presents them in an incomplete and distorted manner. We would like the entire context of our conversations to be presented in the report. It is the Department's position that the Growers are best qualified to determine how market order funds should be spent. Grower interests are represented by the association and advisory boards, which are comprised of growers. Another point made to the audit team that seems to have been ignored is that the Apple Association is not a State operation financed with taxpayer dollars. The nature of the activities they engage in are different than what the auditors are used to and certain expenditures, while not appropriate for a State operation, are appropriate for the Association to incur in carrying out their mission.

\*  
Note  
13

We believe that the expenditure guidelines set forth in the contracts that expenses be used to promote, advertise and publicize New York apples and apple products are sufficient. Exactly what type of criteria the report suggests we develop is unclear since we cannot find anything in the Comptroller's

---

\*See State Comptroller's Notes, Appendix C

expenditure guidelines for State agencies that reflect the level of detail the auditors seem to be requesting.

**Subcontracts**

The Department will require the Associations to enter into written subcontracts and better document the use of competitive bidding. To say that competitive bidding is not used at all is a misstatement of fact.

\*  
Note  
7

**Expenditure Documentation**

As stated previously, the Department has an effective system in place to monitor contractor performance and ensure grower money is spent appropriately. The Department requires that each Association voucher be accompanied by a listing itemizing each expenditure including payee, check number, date and amount. The Department reviews the vouchers and supporting documentation and when warranted questions certain expenditures. This is only the first of many steps in the control process, not the only one as the report conveys. For reasons cited previously, it is not practical to require every contractor we do business with to submit invoices, canceled checks, payrolls and other original forms of documentation with each voucher. The Department is not aware of any goods or services that the Associations claimed as being received that were not. The audit team should not expect the same level of formality from a small not-for-profit organization that they do from a State agency. Unless the audit team can document that goods and services were not received, we are acting in a reasonable manner by relying on the Associations' independent auditor's assessment of the internal control structure that found no reportable conditions.

\*  
Note  
8

**Expenditure Guidelines**

The issue of establishing expenditure criteria was addressed previously. We are now requiring the Association to document the need to exceed allowable

---

\*See State Comptroller's Notes, Appendix C

per diem rates. There is no explanation in the report as to under what circumstances meal per diems were exceeded or expenses for liquor were incurred. When incurred in the course of business related functions, such as having dinner with a grocery chain buyer, we see no basis for the objection.

**Internal Control Weaknesses**

We remain concerned about the focus of this section which seems to want the Department to micro manage the Associations' operations right down to a level of detail where we define employee duties and responsibilities and determine whether a signature stamp is appropriate to sign checks.

We did, however, forward your comments regarding internal controls to the Associations. They responded that several statements in the report are inaccurate. On the rare occasion when use of the signature stamp is necessary, it is the Executive Assistant, not the Accounting Clerk, that affixes it. Therefore, the statement that the same person is effectively providing both signatures is incorrect. This is only done on an individual case basis when necessary to ensure uninterrupted financial operations of the associations.

While the report does acknowledge that it is difficult to ideally separate duties within such a small organization, it does not offer any constructive recommendations in the draft report as to how duties could be better separated. Also, the report states that there are no compensating controls in place to mitigate this inherent risk in a small organization. To the best of our knowledge, the audit team did not discuss this matter with the Associations' independent auditor who would consider the internal control structure in planning and conducting the annual audit. Since there have been no reportable conditions included in the audit report, the Department is acting reasonably. The Associations reported that they asked their independent accountant to place special emphasis on reviewing controls during the 1997-98 audit. They reported to the Boards that controls were found to exceed those of organizations of a similar size.

\*  
Note  
14

\*  
Note  
15

---

\*See State Comptroller's Notes, Appendix C

**Recommendation**

3.) With the exception of requiring the Associations to enter into formal contracts for major purchases of goods and services, we disagree with the remaining parts of the recommendation since accurate books and records are already being maintained, competition for major purchases is solicited, adequate documentation is submitted for pre-audit purposes, expenditure criteria is sufficient and internal controls adequate.

**Grower Associations' Expenses**

To reiterate a point made earlier, the audit team needs to recognize that the Associations are not government operations and that certain entertainment related expenses, while not appropriate for a State agency, are completely legitimate for them to incur. This includes the items listed in the report which are of an insignificant dollar amount.

\*  
Note  
16

The Department has reviewed the expenses questioned by the audit team and, with the exception of a \$42.53 personal expense that slipped through the Association's expenditure review process, found them to serve a legitimate business purpose. Taking isolated instances where a document was misfiled and saying the entire control system is weak does not recognize that an internal control system is designed to provide "reasonable, but not absolute" assurance. The Department will require reimbursement for any expenses not incurred for legitimate market order business.

The \$1,686 Cherry Association expense inadvertently charged to the Apple Association will be reimbursed.

The report does not present any basis or rationale for recommending that the Department pay the Apple Association's dues to national and international trade organizations directly. The New York Apple Growers Association is a member, not the Department. Also, the report does not make clear what its

\*  
Note  
17

---

\*See State Comptroller's Notes, Appendix C

objection is to the Apple Association President traveling to Europe to promote New York apples.

We find no basis for the report's conclusion that the Associations' employees have unreasonable salary and benefit packages. There is no correlation whatsoever between the salary of the Associations' President and the Commissioner's salary and a comparison should not be made. A better comparison would be with other similar trade groups. The Associations' Boards must set compensation levels at a competitive level to attract quality people and in their judgment believed the salary levels set were necessary and appropriate. We have no reason to think otherwise. The audit team needs to remember that the money to pay these salaries is coming out of the Board members own pockets. No purpose is served in disclosing confidential salary information on Association employees.

\*  
Note  
18

There is no rationale presented in the report as to why the audit team feels certain expenses incurred were inappropriate or excessive. The report should recognize that the Associations are non-governmental in nature and have a different business purpose than a State agency.

\*  
Note  
16

Certainly any expense not incurred on market order business is not allowable under the contract and reimbursement will be required. There was, to our knowledge, only one instance where spouse travel was inadvertently paid and has since been reimbursed.

Purchases of the vehicles in question were approved by the Association's Board as part of individual employee compensation packages. While vehicles are available for personal use, reimbursement is made by the employee in accordance with IRS guidelines. Again, this fact is left out of the report.

\*  
Note  
19

**Recommendations**

- 4.) Agree.

---

\*See State Comptroller's Notes, Appendix C

5.) Disagree. Department's current methods for reviewing contractor performance is sufficient.

#### **Department Administrative Expenses**

The Department finds no basis in fact to the conclusions drawn in this section. The Department maintains an excellent cost accounting system for monitoring expenses which, as stated previously, was developed due to the inability of the State's Centralized Accounting System to provide timely and useful financial data with which to administer the Program.

Using figures cited by the audit team in the report, the Apple Research and Development Program administrative expenses did not exceed the 5 percent allowed in 1995-96. The report states actual administrative expenses charged to the Order were \$12,467 while the allowable amount was only \$11,031 (5% of \$220,626) for an excess of \$1,436. The \$12,467 amount, however, still includes \$1,500 paid Cornell University to published research results in the Cornell Fruit Quarterly. Taking the payment to Cornell into account results in no over charge. The Department is not claiming that this amount was paid to Cornell - it is a fact.

The report incorrectly concludes that the Department undercharged the orders for administrative costs incurred. This continues to reflect a lack of understanding of the purpose and terms of the orders and the Department's overall mission to promote the interests of agriculture in New York State. As cited above, the orders clearly state that the "total amount of budgeted administrative costs shall not exceed five percent". There is no requirement that the Department budget the entire five percent. It is entirely within the scope of the Commissioner's discretion to budget none or only a portion of the five percent if the Commissioner believes the funds would be better spent in other areas. Department resources are used in promoting a wide variety of other agricultural commodities which are not covered by marketing orders. The

\*  
Note  
20

Department is entitled to charge up to five percent, not a flat five percent regardless of whether the expenses were incurred or not.

This section of the report again uses selective portions of discussions with the audit team and responses to prior versions of the preliminary audit comments to present an incomplete and biased view. We again express serious concern over the context in which conversations and written correspondence are being misrepresented in the report.

* <b>Note</b> 2
-----------------------

**Recommendation**

6.) Disagree. It is at the Commissioner's, and not the Comptroller's, discretion to determine what, if any, administrative expenses are charged to each order.

**Revenue and Accounting Controls**

Ideally, major processing duties should be separated among different employees. The Department instituted alternative controls to mitigate the situation involved in having one employee perform all of the major functions. An employee of the Finance Office has been assigned responsibility for overseeing the accounting activities for the marketing orders. This employee reviews the monthly financial statements and reconciliation between marketing order accounting records and Finance Office records. The Marketing Order Administrator is also required to periodically verify the accuracy of the detailed accounts payable and accounts receivable records and reconcile them to the control accounts.

While the employee responsible for maintaining market order accounting records does not have a formal accounting degree she has been provided with detailed written procedures and appropriate assistance when needed. Her bookkeeping activities are overseen by an accountant in our Finance Office.

---

*See State Comptroller's Notes, Appendix C
--

There is no prohibition that precludes internal auditors from providing advice. The report vastly overstates the Internal Auditor's involvement in marketing order recordkeeping. There are occasionally unique transactions that transpire which require the Internal Auditor's opinion on how they should be handled. This occurs very infrequently and sometimes not at all during any given year. The Finance Office accountant remains the primary source for assistance. To say that this compromises the Internal Auditor's independence reflects a lack of understanding of the Internal Auditor's role in an organization.

We are unclear as to the point the report is trying to make in this section regarding the Internal Auditor not having conducted an audit of the market orders since 1992. The sole reason audits have not been conducted since 1992 is because your Office has conducted three such audits and to conduct another would be redundant.

We disagree with your statement that marketing order financial reports are not prepared in full conformance with generally accepted accounting principles. It is not possible to record expenses the date they are incurred by the contractor since we do not know that they were in fact incurred until we receive the voucher. When the voucher is received, expenses are in fact recorded in the correct accounting period. At year end the books are kept open until we are reasonably sure all vouchers have been received.

The Department believes that preparation of the balance sheet and income statement for each order provides a sufficient level of financial reporting control and that a statement of changes in fund balance is not necessary or required. The Department is under no obligation to maintain a balance sheet, income statement or statement of changes in fund balance for each order since the financial activity is already included in the State's financial statements. Any statements other than those produced by the State's Centralized Accounting System are done of our own volition. The report should be commending our efforts in this area, not criticizing them.

* Note 21
-----------------

---

*See State Comptroller's Notes, Appendix C
--

**Recommendations**

7.) Disagree. The cost involved in hiring additional staff to fully separate employee duties exceeds the expected benefits.

8.) Disagree. We believe the current employee is capable of maintaining the market order financial records. An Accountant in our Division of Fiscal Management already oversees the market order accounting function and has done so for years.

9.) The Department does conduct periodic audits of the market orders as warranted. It does not, however, see the need to conduct an audit of a program recently audited by other auditors.

10.) Disagree. Market Order balance sheets and income statements are already prepared in conformance with generally accepted accounting principles.

* Note 22
-----------------

---

*See State Comptroller's Notes, Appendix C
--

---

---

# State Comptroller's Notes

---

---

1. Department officials' suggestion that the audit took nearly four years and involved several preliminary and draft reports, is misleading. The Department is mixing a prior audit of the marketing order financial statements with this audit of the Department's administration of the marketing orders. In addition, the delays issuing this report were caused to a large degree by the Department's own actions. During the course of the audit, we provided preliminary copies of matters discussed in this report to Department officials in an attempt to resolve factual differences and to help ensure the report would be fair, complete, and objective. We considered the Department's responses to our preliminary findings, as well as their comments at the closing conference, when preparing our draft report. However, the Department's response to our draft report contained misleading and inaccurate statements, including numerous references to matters that were not contained in the draft. We engaged discussions with Department officials to resolve these differences, revising our draft report and allowing the Department to revise its response. Unfortunately, the Department's revised response (Appendix B) continues to include statements that misrepresent many of our observations and conclusions.
2. The Department's responses to preliminary copies of matters discussed in this report were considered by us in preparing the draft report and the subsequently revised draft report. Department officials apparently did not recognize this or chose not to recognize this when they prepared and submitted their response. Consequently, the Department's response (Appendix B) addresses matters that were not contained in the revised draft report or ignores comments that were included (see Notes 5, 9, 10, 12, 17, 18, 19, 21 & 22 below).
3. The scope of this examination is April 1, 1995 through June 30, 1997, which would account for the absence of 1998 sales information.
4. Department officials contend that the "evaluation of performance against contract objectives is continuously monitored . . ." As discussed in the body of the report, the audit found this statement to be without support. For example, the Department's 1996-97 fiscal year contract with the Apple Growers Association included specific marketing objectives that called for increasing the sale of New York State-grown apples by specific percentages annually in various regions of the country and abroad. The audit found that the Department did not obtain sales information to assess the Apple Growers Association's success at meeting those and other contract goals. For example, the contract has fresh apple sales goals for specific groups of states but the Association's report shows aggregate national sales data. Also, no data is presented regarding the contractual objectives for processed apples.
5. The Department's statement that the previous version of the draft report contained the conclusion that the sour cherry marketing order is no longer needed, is not correct. There was no such conclusion therein, nor is there one in this final report.
6. Department officials contend that "the report presents no credible evidence that expenditures incurred by the grower associations under their respective contracts were unnecessary and unreasonable." The audit identifies expenses that either were not documented, were costly, or may not have been necessary and prudent to promote the purpose of the marketing orders. Among the examples cited in the report are more

---

than \$9,000 for expenses for which there was either no supporting documentation or that was not explained on expense reports.

7. Regarding competitive bidding, the audit found no indication that the growers associations competitively bid major purchases. In addition, appropriate and formal documentation for competitive bids is important for good internal controls. Without adequate control, the Department cannot have adequate assurance that business is conducted properly and the potential for fraud and abuse is reduced.
8. The Department has a fiduciary responsibility to the growers, which should necessitate a higher degree of accountability. In recognition of this responsibility, the Department's Marketing Order Manual states that the Department's Marketing Order Administrator must review paid invoices before approving payment vouchers to the contractors. However, the level of information the Department currently receives from the growers associations is clearly insufficient for the Department to place any reliance on the accuracy of claimed expense information. It also does not provide sufficient detail to identify the nature of many expenses that the Department reimburses. We direct Department officials to the body of the report. We found that documentation is not requested or submitted and recommend that the associations be required to periodically submit supporting documentation with selected vouchers. Periodic submissions of support for selected vouchers should not be overwhelming to either the growers associations or the Department.
9. The revised draft report that the Department responded to, as well as this report, clearly states what is permitted under the Sour Cherry Marketing Order (see page 2 of the report). We fail to see the basis for the Department's comment.
10. The comments attributed to the Marketing Order Administrator regarding contract goals had not been included in the revised draft report which Department officials have responded to. Why Department officials continue to refer to them is unclear.
11. We discuss the Marketing Program Report on page 8 of this report. We conclude that the Marketing Program Report does not assess actual performance to the contractual objectives. Although the Apple Growers Association presents sales information to the growers during the annual apple growers meeting, the information does not match the sales goals set forth in the growers association contract. For example, the contract has fresh apple sales goals for specific groups of states but the Association's report shows aggregate national sales data. Also, no data is presented regarding the contractual objectives for processed apples.
12. The revised draft report that the Department responded to, as well as this final report, states clearly on page 9 that, "Department statistics suggest that there is no excess capacity for New York State apples or sour cherries - all available crop harvests permitted to be sold are sold. However, there is the potential to increase the amount of fresh fruit sales." It also states on page 8 that, ". . .because fresh applies sell at a higher price than apples which are processed, there are opportunities to increase sales of fresh apples." Why the Department has ignored this is unclear.
13. Department officials state that the report takes selective portions of the Department's discussions with the audit team and presents them in an incomplete and distorted manner. We believe the entire context of the

---

Department's position is fairly presented in the report. The Department's response to this issue, on the other hand, neglects to address our observations regarding the Department's fiduciary responsibility.

14. We continue to question the use of a signature stamp to sign checks in the absence of the Assistant Treasurer, thereby negating the control feature of dual signatures.
15. Department officials state that the report does not offer any constructive recommendations as to how duties could be better separated. We direct Department officials to pages 17 and 18 of the report where we suggest the Department institute compensating controls such as having an independent bank reconciliation and providing supervisory review and oversight.
16. Although the growers associations are not governmental agencies, they are not-for-profit corporations that have entered into contractual agreements with the Department. The Department has a fiduciary responsibility to ensure that costs claimed by the associations are allowable, documented, and incurred for services funded under the contractual agreements.
17. The Department's statement concerning national and international dues is unclear. No such recommendation was included in the revised draft report the Department responded to, nor does such a recommendation appear in this report.
18. The Department's statement concerning salaries of association officials is not correct. No such comment was included in the revised draft report the Department responded to, nor does such a comment appear in this report.
19. Contrary to the Department's statement, the information in this paragraph was included in the revised draft the Department responded to, and is included in this report (see page 20). Why Department officials continue to state that this information is left out of the report is not clear.
20. Although Department officials informed us that the \$1,500 was paid to Cornell University, they did not provide us with documentation to support their claim.
21. The Department's statements concerning the Internal Auditor are not accurate. No such comment was included in the revised draft report to which the Department responded, nor does such a comment appear in this report.
22. The revised draft report submitted to the Department for comment did not contain the recommendations listed as 8 and 9 in the Department's response to that revised draft. It is unclear why the Department responded to them.