

Approved

Date

*Fred A. Kerr* 1/20/83

MINUTES OF THE SENATE COMMITTEE ON AGRICULTURE AND SMALL BUSINESS

The meeting was called to order by Senator Fred Kerr at  
Chairperson

10:00 a.m. ~~on~~ Wednesday, January 19, 1983, 1983 in room 423-S of the Capitol.

All members were present ~~except~~

Committee staff present: All were present.

Conferees appearing before the committee: Marvin Webb, Director, Kansas State Grain  
Inspection Department  
Sam Reda, Chief of Warehouse Division

Senator Kerr called the meeting to order. Senator Gannon moved, seconded by Senator Karr, that the January 18, 1983 minutes be approved. Motion carried.

Senator Kerr stated today we would be hearing from Marvin Webb in response to the Interim Committee's letter of December 9, 1982, requesting the KSGID to present a progress report early in the session as to improvements in the department's procedures, resulting from the Post Audit's performance audit. (Note Attachment 1)

Marvin Webb presented his response as contained in Attachment 2, reading therefrom, and called on Sam Reda to assist him in giving the answers to questions posed in the Post Audit report.

Answering Senator Warren's question relative to the impact of the PIK program and if it is successful would the elevators handle as much grain, Mr. Webb replied with the PIK program and the 3-year reserves it would curtail elevator activities but that could not be determined at this time.

Mr. Webb stated they were having an examiner's meeting on January 20 and a number of the suggestions undoubtedly will be implemented including checking of individual settlement sheets at random in their examination procedure and they will begin to trace selected tickets to the Daily Position Record. The test of numerical accounting of tickets is and has been done in the past.

Mr. Reda stated they do have a working agreement with insurance and bonding companies and they receive many calls therefrom. Mr. Webb stated premiums are low on bonds so bonding companies do not seek warehouse bonds only but prefer to have the insurance business also. Mr. Reda stated the federal has a maximum bond of \$500,000, whereas Kansas does not have a maximum. Senator Kerr pointed out the interim committee did not recommend increasing the bond requirement.

The meeting was adjourned.

SENATE

AGRICULTURE AND SMALL BUSINESS COMMITTEE

10:00 a.m., Room 423-S

WEDNESDAY, JAN. 19, 1983

Date

NAME

ADDRESS

ORGANIZATION

Marvin R. West		Ks Grain Growers
Ivan W. Wyatt	McPherson	Ks Farmers Union
Ken Spaul		Gov. office - Policy
George L. Smith, editor		Kansas Farmer
John Blythe	Manhattan	K F B
Gerald Riley	Topeka	K.A.W.G.
Bary Swanson	Lawrence	Gov. office

STATE OF KANSAS

HOUSE OF  
REPRESENTATIVES

December 9, 1982

WILLIAM M. BEEZLEY  
REPRESENTATIVE, FOURTH DISTRICT  
CRAWFORD COUNTY  
ROUTE NO. 2  
GIRARD, KANSAS 66743

Mr. Marvin Webb, Director  
Kansas State Grain Inspection  
Department  
535 Kansas Avenue  
BUILDING MAIL

Dear Mr. Webb:

This letter is in response to action taken by the 1982 Special Committee on Agriculture and Livestock at the November meeting. As you know, at that time the Committee voted to call upon your Department to respond to the standing Agriculture Committees sometime during the beginning of the 1983 Session with a progress report. This report is to indicate the actions your office has undertaken with regard to the recommendations contained in the Legislative Division of Post Audit's performance audit of your Department. I am sure the standing Committees will be interested in your responses, and will be in contact with you to make arrangements for your report.

Sincerely,

A handwritten signature in cursive script that reads "W. M. Beezley".

William M. Beezley, Chairman  
Special Committee on Agriculture  
and Livestock

Atch. 1

JOHN CARLIN  
GOVERNOR  
MARVIN R. WEBB  
DIRECTOR

THE STATE OF KANSAS



GRAIN INSPECTION DEPARTMENT  
GENERAL OFFICE

535 KANSAS AVE., TOPEKA, KANSAS 66603

WAREHOUSE DIVISION  
PHONE (913) 296-3454

INSPECTION DIVISION  
PHONE (913) 296-3451

INSPECTION POINTS	
ATCHISON	KANSAS CITY
COLBY	SALINA
DODGE CITY	TOPEKA
HUTCHINSON	WICHITA

PRESENTATION OF  
MARVIN R. WEBB  
BEFORE  
HOUSE AGRICULTURE & LIVESTOCK COMMITTEE

ROOM 423-S, CAPITOL BUILDING

TOPEKA, KANSAS

ON

JANUARY 19, 1983

Mr. Chairman and Members of the Committee:

I am Marvin R. Webb, Director of the Kansas State Grain Inspection Department.

As requested by Representative Bill Beezley, Chairman, Legislative Special Interim Committee on Agriculture and Livestock, I am submitting our plans for implementing the recommendations made by the Legislative Division of Post Audit.

*Atch. 2*

Hearing cont'  
January 19, 1983

In the Audit Report, Mr. Richard Brown, Legislative Post Auditor, mentioned several thoughts which we believe are significant. One, in particular, which I quote, "Like many other kinds of regulation, licensing and examining, grain warehouses cannot guarantee that failures will not occur". This is the very essence of statements I have made many times. We recognize that changes need to be made and we are perfectly willing and desirous of making improvements in our examinations and regulations, wherever possible. We certainly do not believe we should offer any false hope, to anyone, that more stringent rules, regulations or surveillance will deter the willful fraud or conversion of grain. The two elevator failures in 1982 were both instances of fraud and concealment of records. We are implementing stricter enforcement measures in all phases of our work. We expect to increase our efforts of cooperation with law enforcement agencies and other agencies, in order to know of any unusual events connected with any elevator operation.

Also, I would like to make it quite clear that we have every intention of following the recommendations of the Post Audit report. We cannot implement every recommendation immediately, as suggested, due to the cost factor or other prohibitives.

A staff meeting with our warehouse examiners is scheduled for tomorrow. During this meeting, we will outline in detail the changes in examination procedures which we are implementing now.

Hearing cont'  
January 19, 1983

We have given you a copy of our plan for implementing the recommendations developed by the Legislative Division of Post Audit. While it might appear that we are being somewhat reluctant to agree to some of the recommendations, it is not because we wish to be uncooperative, but instead, due to the inability to fund the increased expense or because we feel it would be unproductive.

It is the responsibility of the Director of the Kansas State Grain Inspection Department to gain and retain the complete confidence of the grain trade and producers. I, as well as past directors, have worked hard to be aware of the problems and concerns of the individual grain firms, so that the department can serve the industry in the most efficient manner. In order to properly perform the functions of a regulatory agency and since the department is concerned with the inspection of the grain, as well as auditing the records and measuring the grain in the warehouses of Kansas, we must develop and maintain a close relationship with the officers and staff of the various Boards of Trade and the individual grain firms. It is our belief that we have the respect of the grain trade, partly because we have worked so hard to show our concern for their many problems, such as: 1) low market prices, 2) lack of foreign sales, and 3) storage problems, just to mention a few.

As a result of our concern regarding elevator failures in the State of Kansas, a Task Force was formed to study these problems. Mr. Bill Morand,

Hearing cont'  
January 19, 1983

President of Collingwood Grain, Inc., was chairman of the Task Force which was composed of twelve members of the grain trade. The other highly respected members were :

Peggy Gatton, Kan-Ag Grain Terminal Co., Parsons, KS  
Gary McKinney, C.G.F. Topeka Grain Elevator, Topeka, KS  
Don Millikan, Wright-Lorenz Grain Co., Salina, KS  
Stan Simpson, Dodge City Coop Exchange, Dodge City, KS  
Robert Smith, Evans Grain Co., Salina, KS  
Francis Gwin, Farmway Coop, Inc., Beloit, KS  
Erwin Schrag, Jr., Alexander & Alexander, Inc., Kansas City, MO  
Tom Wilson, Lynch Grain Co., Salina, KS  
John Johntz, Cereal Food Processors, Wichita, KS  
John Hirsch, Garvey Elevator, Inc., Wichita, KS  
Jim Frost, Continental Grain, Kansas City, MO

We are very proud of the 86 year record of continuous operation of the Kansas Grain Inspection Department. We expect to do everything possible to maintain the reputation for being an outstanding inspection department in the nation. We, of course, are ever mindful of the need to change with the times and improve our procedures. We are in changing times and stressful times. The grain dealers have no idea what is going to happen these next few months. We don't have any idea how seriously our business will be affected by the three year reserve program, or the PIK program or foreign sales. Are we going to be able to sell additional grain overseas? Any or all of these programs can seriously affect our income,

Hearing cont'  
January 19, 1983

as the greater amount of our income is derived from the inspection service and it is a voluntary program. It is very possible the movement of grain will be very limited. We, of course, have increasing cost in the warehouse division.

We have a sincere desire that the committee fully understand we are concerned about the proper operation of all grain elevators in the State of Kansas, just as you committee members are. We are mindful of economic conditions and the bankruptcies that are occurring in all business nationwide. While any elevator failure is a terrific blow to any community, we have been fortunate that failures are as few as they are in our state.

Now, if you have any questions, I will attempt to answer them.

I thank you for the opportunity to appear here this morning.



KANSAS STATE GRAIN INSPECTION DEPARTMENT  
AUDIT RECOMMENDATIONS AND AGENCY IMPLEMENTATION

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AUDIT RECOMMENDATIONS FOR IMPROVING LICENSING PROCEDURES

AND KSGID IMPLEMENTATION

1. (Audit) To obtain more thorough information for evaluating the financial condition of grain warehouses, the Grain Inspection Department should do the following:
  - a. (Audit) Seek a change in Kansas Administrative Regulations to require that financial statements be prepared in accordance with generally accepted accounting principles. As a result of this change, the financial statements submitted should include a balance sheet, a statement of income, a statement of retained earnings, and a statement of changes in financial position.
  - a. (KSGID Implementation) As proposed in Senate Bill #1, we are supportive of amending Kansas Administrative Regulations to require the same financial information as is now being required by Agricultural Marketing Service, U.S.D.A.
  - b. (Audit) Seek a change in Kansas Administrative Regulations to require that the financial statements be accompanied by an audit or review report conducted by an independent certified public accountant or an independent public accountant. Such an audit or review should be carried out in accordance with standards of the accounting profession.
  - b. (KSGID Implementation) Every application for a public warehouse license shall be accompanied by a current financial statement. The statement shall include such information as required by the director to administer and enforce the public warehouse laws of this state, including but not limited to a current balance sheet, statement of income (profit and loss), statement of retained earnings and statement of changes in financial position. The applicant shall certify under oath that the statement as prepared accurately reflects the financial condition of the applicant as of the date specified and fairly represents the results of operations of the applicant's public warehouse business for the period specified. The financial statement shall be accompanied by: (1) A report of audit or review conducted by an independent certified public accountant or an independent public accountant in accordance with standards established by the American institute of certified public accountants and the accountant's certifications, assurances, opinions, comments and notes with respect to the statement; or (2) a compilation report of the financial statement, prepared by a grain commission firm or management firm which is authorized pursuant to rules and regulations of the federal commodity credit corporation to provide compilation reports of financial statements of warehousemen.

SB 1

- c. (Audit) Seek a change in Kansas Administrative Regulations to require that license applications be submitted within 90 days of the end of the warehouse's fiscal year, meaning that the financial statement will be no more than 90 days old.
- c. (KSGID Implementation) This recommendation would be ideal but would be impractical because approximately 35% of the licensed elevators have their fiscal year end on December 31. It is our policy, at this time, to issue licenses on a staggered basis eight months out of the year. We are now asking for an updated financial statement, if the one submitted at application time is over 90 days old. It is our recommendation that we should continue our current policy of issuing licenses on a staggered basis; but we will analyze the new statement, when received, and request additional bond if this statement reflects a lesser net worth than the statement used at the time the license was issued.
2. (Audit) To ensure that financial information submitted by grain warehouses is analyzed adequately, the Grain Inspection Department should develop specific tests and analyses to be conducted. Examples would include developing various kinds of financial ratios for warehouses, comparing a warehouse's information with standards and norms, and analyzing the changes in a warehouse's condition over a period of several years. The Department should also develop a plan for ensuring that the staff responsible for licensing has the necessary expertise to analyze the information in financial statements and that the analysis is adequately reviewed.
2. (KSGID Implementation) The Grain Inspection Department will begin using ratios that have been developed, beginning in January 1983.
- As of 1-17-83, the present personnel has been enrolled in additional studies in the field of accounting.
3. (Audit) To ensure that all State-licensed grain warehouses have adequate insurance against fire, explosion, lightning, and tornadoes, the Department should review the adequacy of insurance coverage before it issues a license as well as during subsequent evaluations.
3. (KSGID Implementation) We feel that our department is currently performing adequate surveillance of insurance policies and reported amounts during our examinations. Also, on all new entities, and prior to the licensing and bonding, the warehouse examiner completes a Form TW-369, Warehouseman's Insurance Coverage.

*Checked more than once a year.*

RECOMMENDATIONS FOR IMPROVING FINANCIAL PROTECTION FOR  
GRAIN PRODUCERS AND KSGID IMPLEMENTATION

1. (Audit) To provide greater protection to the individual grain producer, the Grain Inspection Department should seek a change in Kansas Administrative Regulations to require a warehouse to have a minimum net worth. Any differences between the minimum net worth for all warehouses and the net worth required for a particular warehouse's capacity should be made up through an increase in bond.
1. (KSGID Implementation) This has been covered by Senate Bill #1, beginning with line 67.
2. (Audit) To provide greater protection to the individual grain producer, the Legislature should consider raising bond requirements for grain elevators. Specifically, the Legislature should consider amending K.S.A. 34-229 to require the use of a 25 percent factor in the formula for determining bond requirements rather than a factor of 15 percent. The Legislature should also consider raising the limit at which a lower multiplier is used to \$300,000 instead of the current \$200,000, and it should consider raising the lower multiplier to 1½ percent instead of the current 1 percent.
2. (KSGID Implementation) The present Kansas bonding requirements are among the highest in the country. We feel that additional bonding would cause extreme hardship on the industry, due to the higher cost of bond premiums, and could result in causing smaller operations to go out of business.

Also, with Kansas' higher bond requirements, many elevators would seek a federal license which would lower the protection to the producer.

AUDIT RECOMMENDATIONS FOR IMPROVING EXAMINATION PROCEDURES

AND KSGID IMPLEMENTATION

To help ensure that warehouse examination procedures are adequate for protecting grain producers, the Department should do the following:

- a. (Audit) Test the mathematical accuracy of individual settlement sheets.
- a. (KSGID Implementation) After our examiner's meeting, January 20, 1983, we will incorporate the test of individual settlement sheets in our examination procedure. *will be at random.*
- b. (Audit) Trace selected scale tickets to the daily position records and test the numerical accounting of scale tickets.
- b. (KSGID Implementation) We will begin to trace selected tickets to *daily position* D.P.R. *record* after our examiner's meeting. The test of numerical accounting of tickets is and has been done in the past.
- c. (Audit) Test the mathematical accuracy of the daily position records and trace transactions posted in the daily position records to supporting documents.
- c. (KSGID Implementation) As above, after our examiner's meeting, we will test the mathematical accuracy of the D.P.R.
- d. (Audit) Test "out bound" scale tickets as well as "in bound" tickets.
- d. (KSGID Implementation) The issuance of "in bound" scale tickets or receipts to the producer establishes the firm's liability. Therefore, "in bound" scale tickets are very necessary.

The "out bound" scale tickets will not reflect the liability of the elevator due to the fact that the "out bound" scale ticket probably would not be issued if fraud was involved.

- e. (Audit) Increase the number of scale tickets and summary sheets tested at larger warehouses.
- e. (KSGID Implementation) Serious consideration will be given to increasing the number of scale tickets tested, insofar as time will allow.

AUDIT RECOMMENDATIONS FOR IMPROVING ENFORCEMENT  
AND KSGID IMPLEMENTATION

1. (Audit) To help protect grain producers against warehouse failures, the Grain Inspection Department should make the following changes in its enforcement practices:
  - a. (Audit) Begin requiring examiners to document on examination forms any apparent violations of the Public Warehouse Law and any factors leading up to those apparent violations.
  - a. (KSGID Implementation) We will instruct our examiners to provide documentation of apparent violations of our law and the factors leading to same.
  - b. (Audit) Begin requiring examiners to document their follow-up on prior deficiencies addressed during a subsequent examination.
  - b. (KSGID Implementation) In the past, we have documented the corrections on any prior exceptions, but we will require a more detailed documentation in the future.
  - c. (Audit) Begin requiring special follow-up examinations if examination reports note severe or recurring problems.
  - c. (KSGID Implementation) The Grain Inspection Department is already making special follow-up exams on elevators with severe or recurring problems. We will review the classification of severity in the future.
  - d. (Audit) Begin taking stronger actions, including suspension or revocation of licenses, special examinations, and assessment of fines and penalties, if appropriate to ensure that problems found during examinations are corrected.
  - d. (KSGID Implementation) We will begin reviewing the possibility of stronger action i.e. suspension, revocation and assessment of fine and penalties based on the severity, on a case to case basis.

2. (Audit) To help ensure that examinations are complete, thorough, and consistent, the Grain Inspection Department should begin reviewing completed examinations more extensively and should begin on-site evaluations of examiners.
2. (KSGID Implementation) Chief Examiner III and Field Audit Supervisor II will begin consulting each other on the severity of exceptions noted during an examination and act accordingly on any follow-up.

Beginning immediately, the supervisory examiners will increase and document on-site evaluations of field examiners.

3. (Audit) To ensure that adequate deterrents exist against maintaining false or duplicate records, the Legislature should consider amending the Warehouse Act to make committing such acts a felony and to provide appropriate penalties.
3. (KSGID Implementation) This is presently being submitted by Senate Bill #4.