

REPORT DIGEST

MANAGEMENT AUDIT OF THE

ILLINOIS AQUACULTURE DEVELOPMENT FUND

ILLINOIS DEPARTMENT
OF AGRICULTURE

Released: September 2004



State of Illinois
Office of the Auditor General

WILLIAM G. HOLLAND
AUDITOR GENERAL

To obtain a copy of the report
contact:

Office of the Auditor General
Iles Park Plaza
740 East Ash Street
Springfield, IL 62703
(217) 782-6046 or
TTY (888) 261-2887

This report is also available on the
worldwide web at:

<http://www.state.il.us/auditor>

SYNOPSIS

In Fiscal Years 2000 through 2004, the Illinois Department of Agriculture (Agriculture) distributed \$4,931,000 of State support for aquaculture to the Illinois Fish Farmers Cooperative (Cooperative) located in Pinckneyville, Illinois. Additional State funding of \$2,020,000 was provided as capital support for the Cooperative's fish processing plant.

Operations at the fish processing plant began in October 2001 and continued until the plant was formally shut down in September 2003. Legislation passed by the General Assembly on July 24, 2004, and signed by the Governor on July 30, 2004, abolished the Illinois Aquaculture Development Fund effective August 31, 2004 (Public Act 93-839). The audit concluded the following:

- The Cooperative did not have an adequate business plan, and the plan that was developed was not completed until January 2001, in the middle of the second year in which the Cooperative was receiving State funding for operations and capital. At that point, the Cooperative had already received over \$3.2 million in capital and operating grant funding from the State.
- We identified some expenditures of the Illinois Fish Farmers Cooperative that were questionable for an entity receiving substantial State support. Those included taking a loss for fish farmers, expenditures for a shrimp festival, some meal, travel and advertising expenditures, as well as executive payments for relocation and severance.
- Agriculture did not develop administrative rules related to distributing Aquaculture Development Act funds as required by the Aquaculture Development Act (20 ILCS 215/5.5). Establishing adequate procedures and administrative rules could provide additional guidance and structure to the grant program as well as helping to ensure State resources are expended for the purpose intended and that adequate accountability exists.
- The Cooperative generally kept adequate minutes, books, and records, but we did find examples where adequate records were not maintained. We also found documentation that showed that the Cooperative Board refused to make certain information in its records public as required by the Aquaculture Development Act.

REPORT CONCLUSIONS

Since Fiscal Year 2000, the Illinois Fish Farmers Cooperative (Cooperative) received \$4,931,000 of State support for aquaculture from the Illinois Department of Agriculture. The aquaculture support was \$1 million per year from Fiscal Years 2000 to 2003 and \$931,000 in Fiscal Year 2004. In Fiscal Year 2000, the appropriation was from the General Revenue Fund but in other years the support was from the Illinois Aquaculture Development Fund. An additional \$2,020,000 in capital support for the Cooperative's fish processing plant was provided from the General Revenue and Capital Development Funds.

Funding to support aquaculture was established when the Aquaculture Development Act was revised by Public Act 91-530, effective August 13, 1999, to require the Department of Agriculture (Agriculture) to make grants to an aquaculture cooperative from the Illinois Aquaculture Development Fund, a special fund created in the State Treasury. The Act required that each July 1st from 1999 through 2008, the Comptroller order transferred and the Treasurer transfer \$1 million from the General Revenue Fund into the Illinois Aquaculture Development Fund. Legislation passed by the General Assembly on July 24, 2004, and signed by the Governor on July 30, 2004, abolished the Illinois Aquaculture Development Fund effective August 31, 2004 (Public Act 93-839).

With State support, the Illinois Fish Farmers Cooperative developed a fish processing plant along with providing technical services to fish farmers and marketing aquaculture products. Processing operations began in October 2001 and continued until the plant was formally shut down in September 2003. In summary, during Fiscal Years 2000 and 2001 the plant was in the development stages, during Fiscal Years 2002 and 2003 the fish processing plant was operational, and during Fiscal Year 2004 the processing plant ceased operations.

Since the closure of the processing plant, the Cooperative continues to provide technical assistance for fish farmers and assist farmers to find a market for their aquaculture products. With its current operation, the Cooperative does not need its large processing plant and is attempting to sell it. Currently the Cooperative produces some income from member dues, from brokerage fees on fish sales, and from ordering aquaculture equipment and reselling to members. Without State support, other ways of producing income would probably have to be developed for the Cooperative to continue.

The Cooperative did not have an adequate business plan, and the plan that was developed was not completed until January 2001, in the

middle of the second year in which the Cooperative was receiving State funding for operations and capital. At that point, the Cooperative had already received over \$3.2 million in capital and operating grant funding from the State. The Department of Agriculture did not provide documentation that it had requested or reviewed the Cooperative's business plan.

As of April 13, 2004, the Cooperative still had outstanding debt in excess of \$500,000. The debt consisted primarily of three items: first, a loan from the City of Pinckneyville, which is State money passed through the City; second, a loan that is federal money from the USDA Intermediary Relending Program, also passed through the City; and third, a bank note. Cooperative officials hope that the sale of the processing facility building would provide the revenue necessary to pay the loans off.

We identified some expenditures of the Illinois Fish Farmers Cooperative that were questionable for an entity receiving substantial State support. Those included taking a loss for fish farmers, expenditures for a shrimp festival, some meal, travel and advertising expenditures, as well as executive payments for relocation and severance.

Although we questioned some expenditures, those that we reviewed were generally within the statutory purposes of the Illinois Aquaculture Development Act. However, because the statute is written so broadly, it established few limitations on whether expenditures are allowable.

The Illinois Department of Agriculture did not develop administrative rules related to distributing Aquaculture Development Act funds as required by the Aquaculture Development Act (20 ILCS 215/5.5). Establishing adequate procedures and administrative rules could provide additional guidance and structure to the grant program as well as helping to ensure State resources are expended for the purpose intended and that adequate accountability exists.

Audits of the Illinois Fish Farmers Cooperative were performed each fiscal year through 2003 as required. The audits found no instances of noncompliance that would be required to be reported under applicable financial auditing standards.

The Cooperative generally kept adequate minutes, books, and records, but we did find examples where adequate records were not maintained. We also found documentation that showed that the Cooperative Board refused to make certain information in its records public as required by the Act.

The Department of Agriculture did not adequately monitor grants to the Cooperative. It did not consistently use statutory tools that were available including required budget review and required audits. In addition, Agriculture did not assign staff who consistently monitored the grant. It also did not assure that all grant agreement requirements were complied with.

BACKGROUND

On February 17, 2004, the Illinois Legislative Audit Commission adopted LAC Resolution Number 127. The Resolution directed the Auditor General to conduct a management audit of the Illinois Aquaculture Development Fund within the Department of Agriculture. The audit was to include the following determinations with regard to the Aquaculture Cooperative:

- The amount and purpose of expenditures and transfers from the Illinois Aquaculture Development Fund for Fiscal Years 2001, 2002, and 2003;
- Whether expenditures and transfers from the Illinois Aquaculture Development Fund made in Fiscal Years 2001, 2002, and 2003 appear to be in conformity with applicable rules and statutes;
- Whether all minutes, books, budgets and records required under the Act to be kept and made available to the public by the Aquaculture Cooperative have been maintained for Fiscal Years 2001, 2002, and 2003; and
- Whether the financial books and records of the Aquaculture Cooperative were audited by a certified public accountant at least once each fiscal year for 2001, 2002, and 2003, as required by statute. (page 3)

AQUACULTURE DEVELOPMENT IN ILLINOIS

The Illinois Aquaculture Development Act, effective January 1, 1988, was passed to establish a policy and program toward improving the science and husbandry of aquaculture as a means to expand the aquaculture industry and related economic activity in the State. The Act defined “aquaculture” as the controlled propagation, growth and harvest of aquatic organisms, including but not limited to fish, shellfish, mollusks, crustaceans, algae and other aquatic plants, by an aquaculturist.

The Aquaculture Development Act was revised by Public Act 91-530, effective August 13, 1999, to require Agriculture to make grants to an

The Illinois Aquaculture Development Act was effective January 1, 1988.

aquaculture cooperative. The grants would come from the Illinois Aquaculture Development Fund, a special fund created in the State Treasury. On July 1, 1999, and on each July 1 thereafter through July 1, 2008, the Comptroller shall order transferred and the Treasurer shall transfer \$1,000,000 from the General Revenue Fund into the Illinois Aquaculture Development Fund. The Aquaculture Cooperative shall consist of any individual or entity of the aquaculture industry in the State that seeks membership pursuant to the Agricultural Cooperative Act (805 ILCS 315).

In Fiscal Year 2000, the Illinois Department of Agriculture gave the first aquaculture grant to the Illinois Fish Farmers Cooperative.

In Fiscal Year 2000, the Department of Agriculture gave the first aquaculture grant to the Illinois Fish Farmers Cooperative. The Cooperative was organized under the Illinois Agricultural Cooperative Act (805 ILCS 315) and had a board of directors composed of 11 members who were primarily individuals involved in fish farming.

In the fall of 1999 the Cooperative moved into a building in Pinckneyville that had been a warehouse. An engineering firm and a firm that makes fish processing equipment worked with the Cooperative on the design of the plant. Construction for the processing facility began on the approximately 42,000 square foot building around April 2001. Fish processing operations began in October 2001 and continued until the plant was formally shut down in September 2003. In summary, during Fiscal Years 2000 and 2001 the plant was in the development stages, during Fiscal Years 2002 and 2003 the fish processing plant was operational, and during Fiscal Year 2004 the processing plant ceased operations.

The plant was primarily designed to process catfish which was the centerpiece of the Cooperative's initial strategy. The decision to process catfish had been based upon assumptions concerning profitability and growth opportunities. A drop in the prices for catfish came as a result of the decline in the economy following the terrorist attacks of September 11, 2001, and changes in the aquaculture industry.

By October 2002, the processing plant was having significant financial problems.

By October 2002, the processing plant was having significant financial problems. A Cooperative official said they tried everything they could from increasing production to reducing production and focusing on specialized products, but were never able to reach a break-even point.

While the plant was operating, odor from the waste lagoons became a problem for the Cooperative and the processing plant's neighbors. As of May 2004, the Cooperative was waiting for Illinois Environmental Protection Agency to complete inspections of the waste lagoons. One of the lagoons has been cleared of environmental issues. Before it can be cleared by EPA, the other lagoon must have the remaining water and sludge removed. This environmental issue is an obstacle to the Cooperative's efforts to sell the building.

Since the plant's closure, most processing equipment has been sold. As of May 2004, only two pieces of equipment remained. Both were specialized pieces of equipment that are difficult to sell. The Cooperative had retained four vehicles, two pickups used by biologists who provided technical assistance to fish farmers, a minivan, and a refrigerated delivery

Digest Exhibit 1 ILLINOIS FISH FARMERS COOPERATIVE OUTSTANDING LONG TERM DEBT As of April 13, 2004	
Pinckneyville (CDAP and IRP)	\$452,357
Bank Note	<u>\$ 48,382</u>
Total	<u>\$500,739</u>
Note: This does not include various accounts payable of approximately \$50,000. Source: Illinois Fish Farmers Cooperative.	

truck. As of April 13, 2004, the Cooperative still had outstanding long-term debt in excess of \$500,000. Digest Exhibit 1 shows the debt outstanding. The CDAP loan from Pinckneyville is State money passed through the City. The IRP loan is federal money from

the USDA Intermediary Relending Program which is also passed through the City. Cooperative officials hope that the sale of the processing facility building will provide the revenue necessary to pay the loans off. In addition to the long term debt, the Cooperative had accounts payable of approximately \$50,000. These included obligations to a mechanical contractor, a law firm, an accounting firm, and the Illinois Environmental Protection Agency.

According to a Cooperative official, the impact of closing was minimal for fish farmers because most were using live hauls to get their fish to market or had switched to different fish that can be sold live. Since the closure of the processing plant, the Cooperative continues to provide technical assistance for fish farmers and assist farmers to find a market for their aquaculture products. With its current operation, the Cooperative does not need the large plant that it currently has. Currently the Cooperative produces some income from member dues, from brokerage fees on fish sales, and from ordering aquaculture equipment and reselling to members. Without State support, other ways of producing income would probably have to be developed for the Cooperative to continue.
 (pages 3-6)

The Cooperative Business Plan

The late time at which a business plan was developed and the weaknesses that we noted in the plan may have contributed to problems at the Cooperative.

The Cooperative did not have an adequate business plan, and the plan that was developed was not completed until January 2001, in the middle of the second year in which the Cooperative was receiving State funding for operations and capital. At that point, the Cooperative had already received over \$3.2 million in capital and operating grant funding from the State. The Department of Agriculture did not provide documentation that it had requested or reviewed the Cooperative’s business plan.

The late time at which a business plan was developed and the weaknesses that we noted in the plan may have contributed to problems at the Cooperative and may have made it difficult for Agriculture to assess whether releasing grant funding to the Cooperative was appropriate. (pages 7-8)

AQUACULTURE EXPENDITURES

The State provided \$6.95 million to the Illinois Fish Farmers Cooperative from Fiscal Years 2000 to 2004.

Digest Exhibit 2 shows the State’s expenditures to the Illinois Fish Farmers Cooperative for Fiscal Years 2000 to 2004. The Cooperative received a total of \$6,951,000 in State funding. In Fiscal Year 2000, the operating grant money was appropriated from the General Revenue Fund instead of the Aquaculture Development Fund. In Fiscal Year 2001, the Cooperative received a State capital grant in the amount of \$1,220,000. This grant was made to the Cooperative along with the City of Pinckneyville. The grant agreement stated that the funds were to be used for capital costs related to the establishment of a fish processing plant. The Cooperative also received an \$800,000 State capital grant in Fiscal Year 2002 for the same purpose.

Digest Exhibit 2
STATE EXPENDITURES FOR THE ILLINOIS FISH FARMERS COOPERATIVE
 Fiscal Years 2000 to 2004

	FY00	FY01	FY02	FY03	FY04	Total
From the Aquaculture Development Fund		\$1,000,000	\$1,000,000	\$1,000,000	\$931,000	\$3,931,000
From the General Revenue Fund	\$1,000,000 ^A		\$800,000 ^C			\$1,800,000
From the Capital Development Fund		\$1,220,000 ^B				\$1,220,000
Total	\$1,000,000	\$2,220,000	\$1,800,000	\$1,000,000	\$931,000	\$6,951,000

^A The first year’s grant was from the General Revenue Fund instead of the Aquaculture Development Fund.
^B Granted to the Fish Farmers Cooperative and the City of Pinckneyville for capital costs related to the establishment of the fish processing plant.
^C Granted to the Fish Farmers Cooperative for capital costs related to the establishment of the fish processing plant.

Source: Illinois Comptroller and grant agreement information summarized by OAG.

During Fiscal Years 2000 through 2003, the Cooperative's expenditures totaled \$11.9 million. Digest Exhibit 3 shows the percentage of the total expenditures for each category of expenditures. This exhibit is based on financial statements from required audits of the Cooperative. In the first two years of existence, because of grant moneys, the Cooperative's financial statements showed an excess of revenues over expenditures. However, in Fiscal Year 2002, once the fish processing plant became operational, expenditures exceeded revenues by nearly \$700,000. In Fiscal Year 2003, expenditures exceeded revenues by nearly \$500,000.

Digest Exhibit 3 ILLINOIS FISH FARMERS COOPERATIVE EXPENDITURES BY TYPE Fiscal Years 2000 to 2003		
<u>Category</u>	<u>Total Expenditures</u>	<u>% of Total</u>
Purchases of products for resale	\$3,702,679	31.0%
Plant expenses	1,414,272	11.9%
Selling expenses	228,993	1.9%
General and administrative costs:		
Salaries	1,869,341	15.7%
Taxes and benefits	222,381	1.9%
Marketing costs	54,528	0.5%
High School Grants	100,470	0.8%
Grand Opening, Net	14,102	0.1%
Insurance	287,584	2.4%
Office expenses	94,537	0.8%
Legal fees	262,223	2.2%
Accounting fees	147,333	1.2%
Other expenses	173,565	1.5%
Purchase of capital assets	3,323,454	27.8%
Debt service – interest	<u>39,120</u>	<u>0.3%</u>
Total expenditures before taxes	<u>\$11,934,582</u>	<u>100.0%</u>
Source: Cooperative audit data summarized by OAG.		

We identified some Cooperative expenditures that may be questionable for an entity receiving substantial State support. Those expenditures included taking a loss for fish farmers, some meal and travel expenditures, expenditures for a shrimp festival and radio advertising when the Cooperative was experiencing severe financial problems, and executive payments and severance packages for executives when the processing plant failed.

Taking a Loss for Fish Farmers

The Cooperative took a loss totaling \$14,335.53 on three pre-purchased fish contracts, including two with Board members, instead of the producers (fish farmers) taking the losses. Losses taken included \$6,250 and \$1,485 for two Board members and \$6,600 for a non-Board member.

Meal and Travel Expenditures

Expenditure reports for Fiscal Years 2000 through 2003 showed that the Cooperative spent \$7,409 to an account called Meals. Meals were also charged to other accounts such as Sales Meals, Board Meetings, and Miscellaneous Expense. While receipts for the meals were documented, there was no documentation that meals were for a legitimate purpose (such as meeting with potential customers or vendors).

Travel expenditures for Fiscal Years 2000 through 2003 totaled \$39,252. We identified travel expenditures of \$837 for the Executive Director for trips to Boston (March 2003) and New York (August 2003). Both of these trips took place when the Cooperative was struggling financially. We asked the Cooperative for documentation of the purpose of the trips and documentation that the Board minutes showed that expenditures were approved. For the trip to Boston, it appeared that the Cooperative paid for two plane tickets, one for the Executive Director and one for an individual not employed by the Cooperative. Although the trips are listed among expenditures in the Board minutes and reports, the purpose of the trips was never identified. Cooperative officials said the trips were for a seafood show and to meet with a buyer, but no documentation of that could be provided.

Shrimp Festival and Advertising

In Fiscal Year 2004, the Cooperative sponsored a Shrimp Festival at the Du Quoin State fairgrounds. It was held in October 2003 after the fish processing plant had been formally shut down in September 2003. The total cost for the festival was \$12,091. Cooperative officials noted that they intended to generate income from the festival to cover its costs and that revenues of \$3,375 were obtained from donations, booth rentals and games. Although promotion of shrimp farming may be acceptable for an ongoing entity, it seems questionable for the Cooperative that was experiencing severe financial problems. According to an Agriculture official, the Department had planned to participate but decided not to have a booth at the Festival because officials did not want to send any type of message to the Cooperative that the Department might support future Cooperative activities.

In addition to the Shrimp Festival and its associated advertising, the Cooperative also had a contract with a radio group for advertising. The Cooperative eventually paid the radio group \$15,790 for about 12 months, mostly in Fiscal Year 2003. The Cooperative's second executive director tried to cancel the contract in January 2003. Because the Cooperative fell behind in paying the radio advertising bills, there was a dispute over payments. Eventually \$2,359 of the debt was written off.

Executive Payments

The Cooperative made various executive payments for relocation and severance that it may not have been obligated to make. Two executives were paid \$5,000 each for relocation even though their employment agreements did not call for the benefit. In addition, the Cooperative paid \$55,427 as part of executive severance packages even though it may not have been obligated to make these payments.

We recommended that Agriculture and the Illinois Fish Farmers Cooperative ensure that any future expenditures to support aquaculture are adequately planned, appropriate for State purposes, and adequately documented. (pages 12-19)

The Cooperative paid \$55,427 as part of executive severance packages even though it may not have been obligated to make these payments.

COMPLIANCE WITH STATUTORY PROVISIONS

The Illinois Department of Agriculture did not develop administrative rules related to distributing Aquaculture Development Act funds as required by the Aquaculture Development Act (20 ILCS 215/5.5). Establishing adequate procedures and administrative rules could provide additional guidance and structure to the grant program as well as helping to ensure State resources are expended for the purpose intended and that adequate accountability exists. We recommended that Agriculture establish adequate rules and procedures to administer and monitor grants to aquaculture cooperatives, as required by the Illinois Aquaculture Development Act.

Audits of the Illinois Fish Farmers Cooperative were performed each fiscal year through 2003 as required. The Aquaculture Development Act (20 ILCS 215) established the requirement that the financial books and records of the Cooperative shall be audited by a certified public accountant at least once each fiscal year and at other times as designated by the Director. One accounting firm performed each of the annual audits of the operating and capital grants, on a regulatory basis, in accordance with generally accepted auditing standards and standards applicable to financial audits contained in Government Auditing Standards. The audits found no instances of noncompliance that

Required audits of the Cooperative were performed each fiscal year through 2003.

would be required to be reported under the standards. There were no matters involving internal controls over financial reporting and its operations that would be considered material weaknesses. There was one instance of a reportable condition from the Fiscal Year 2000 audit which found that inadequate controls existed with respect to aquaculture grants which were awarded to Illinois high schools. This condition was later remedied by the Cooperative.

Required Budgets and Review

Although Agriculture received budgets from the Illinois Fish Farmers Cooperative for each of the five fiscal years, the Department could only document commenting on three of those budgets. The Aquaculture Development Act requires budgets to be submitted by the Cooperative and reviewed by the Department when grant funding is provided. Budget review is an important element of monitoring Aquaculture grants. Agriculture should assure that all grant funds, particularly those from the Illinois Aquaculture Development Fund, are adequately monitored.

Required Minutes, Books, and Records

The Cooperative generally kept adequate minutes, books, and records, but we did find examples where adequate records were not maintained. We also found documentation that showed that the Cooperative Board refused to make information in its records public. The Aquaculture Development Act requires that “The Cooperative shall keep minutes, books, and records that clearly reflect all of the acts and transactions of the Cooperative and shall make this information public” (20 ILCS 215/5.5).

We noted two examples where records may not have been made available to the public. In Cooperative Board minutes dated April 18, 2000, the minutes reflect that the Aquaculture Advisory Board (created by the Cooperative bylaws) had requested copies of Cooperative Board meeting minutes. The Cooperative Board decided that the minutes would be circulated to Cooperative Board members only with a summary to the advisory board. Also, in letters from November and December 2001, limitations on public access to minutes and financial records are also noted.

We recommended that the Department of Agriculture assure that the Illinois Fish Farmers Cooperative, or other cooperatives receiving Aquaculture Development grants, keep minutes, books, and records that clearly reflect all of the acts and transactions of the Cooperative and make this information public, as required by the Aquaculture Development Act. (pages 21-27)

MONITORING

The Department of Agriculture did not adequately monitor grants to the Cooperative. It did not consistently use statutory tools that were available including required budget review and required audits. In addition, Agriculture did not assign staff who consistently monitored the grant. It also did not assure that all grant agreement requirements were complied with. Without considering over \$2 million in capital grants, Agriculture disbursed a total of \$4,931,000 in Aquaculture Development grants since Fiscal Year 2000 to the Illinois Fish Farmers Cooperative. The grants were made by the Department under the authority and direction of the Aquaculture Development Act (20 ILCS 215/5.5).

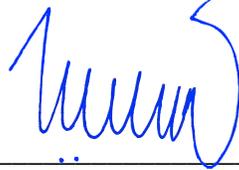
The Department of Agriculture did not adequately monitor grants to the Cooperative.

We recommended that the Illinois Department of Agriculture assure that all grant funds, including those from the Illinois Aquaculture Development Fund, are adequately monitored. This should include reviewing and making changes based on audits, budgets, or other required elements. (pages 28-29)

RECOMMENDATIONS

The audit report contains four recommendations which are noted in this digest. The Illinois Department of Agriculture and the Illinois Fish Farmers Cooperative generally agreed with the recommendations. Appendix I to the audit report contains the complete responses.

The audit also contains one Matter for Consideration by the General Assembly. It is included because Public Act 93-839, passed by the General Assembly on July 24, 2004, and signed by the Governor on July 30, 2004, abolished the Illinois Aquaculture Development Fund effective August 31, 2004. However, references to the Illinois Aquaculture Development Fund remain in the statute, and may need to be amended to conform to the changes made by Public Act 93-839.



WILLIAM G. HOLLAND
Auditor General

WGH\EKW

September 2004

