



Transmitted via e-mail

August 2, 2013

Mr. Dave Preciado, Assistant Director  
Animal Health and Food Safety Services  
California Department of Food and Agriculture  
2800 Gateway Oaks Drive  
Sacramento, CA 95833

Dear Mr. Preciado:

**Final Report—Sparboe Farms, Inc., Egg Quality Control Mill Fee Assessment Reports Audit**

The California Department of Finance, Office of State Audits and Evaluations, has completed its compliance audit of Sparboe Farms, contract 12-0063, for the period July 1, 2008 through June 30, 2011.

Sparboe Farms' response to the report observation and our evaluation of the response are incorporated into this final report. This report will be placed on our website.

We appreciate the assistance and cooperation of Sparboe Farms. If you have any questions regarding this report, please contact Susan Botkin, Manager, at (916) 322-2985.

Sincerely,

Original signed by:

David Botelho, CPA  
Chief, Office of State Audits and Evaluations

Enclosure

cc: Mr. Anthony Herrera, Program Supervisor, Meat, Poultry, and Egg Safety Branch,  
California Department of Food and Agriculture  
Ms. Beth Sparboe Schnell, President, Sparboe Farms, Inc.  
Mr. Craig Boesen, Director of Accounting and Financial Reporting, Sparboe Farms, Inc.

# Audit Report

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## Sparboe Farms, Inc. Contract 12-0063 For the Period July 1, 2008 through June 30, 2011



Source: [www.sparboe.com](http://www.sparboe.com)

Prepared By:  
Office of State Audits and Evaluations  
Department of Finance

**MEMBERS OF THE TEAM**

Susan Botkin, CGFM  
Manager

John Rogers, CPA  
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Final reports are available on our website at <http://www.dof.ca.gov>

You can contact our office at:

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# BACKGROUND, SCOPE, METHODOLOGY AND RESULTS

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## **BACKGROUND**

The California Department of Food and Agriculture (CDFA), Egg Safety and Quality Management Program is the regulatory authority for shell eggs and egg products produced, shipped, or sold in California. The program's mission is to ensure that eggs sold in California are of known quality, origin, grade and size. They also must be properly handled, labeled, transported and refrigerated and are wholesome and safe to eat.

To help fund inspection activities of eggs and egg products within California, the California Food and Agriculture Code section 27551 requires out-of-state egg producers to pay a fee ranging from one half cent (\$0.005) to four and one half cents (\$0.045) per 30 dozen eggs shipped to California.

Sparboe Farms, Inc., operates as a producer and wholesaler of shell eggs. Sparboe Farms was founded in 1954 and its headquarters is located in Wayzata, Minnesota. Sparboe Farms operates egg production facilities in Minnesota, Iowa, and Colorado. Its sister company, Sparboe Foods, operates as a distributor of powdered, liquid, and frozen egg products. Sparboe Farms ships eggs directly to California or sells to distributors who in turn sell the eggs to California. Sparboe Farms is responsible for filing the Out-of-State Egg Quality Control Mill Fee Assessment Reports and remitting the required fees to CDFA.

## **SCOPE**

In accordance with the interagency agreement with CDFA, the California Department of Finance, Office of State Audits and Evaluations (Finance), audited the Out-of-State Egg Quality Control Mill Fee Assessment Reports (Assessment Reports) filed by Sparboe Farms during the three-year assessment period July 1, 2008 through June 30, 2011.

The audit objectives were to determine whether the Assessment Reports filed with CDFA were accurate, complete, and fee payments were remitted in accordance with CDFA requirements.

## **METHODOLOGY**

To determine whether the Assessment Reports were accurate, complete, and in compliance with CDFA laws and regulations, we performed the following procedures:

- Interviewed key personnel and reviewed company policies and procedures to obtain an understanding of the Assessment Report preparation process.
- Reviewed accounting records, sales invoices, and shipping records.
- Selected a sample of Assessment Reports to determine if reported egg counts, sales loss adjustments, and fees calculated were supported, accurate, and in compliance with CDFA laws and regulations.
- Verified fees were remitted to CDFA.

- Performed sales analysis by reviewing company accounting records and matching results to Assessment Reports.

We also reviewed the California border station reports collected by CDFA for the three fiscal years. However, due to a high percentage of egg shipments classified as coming from unknown shippers, we were unable to match the border reports to the Assessment Reports.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our observations and recommendations based on our audit objectives. We believe the evidence obtained provides a reasonable basis for our observations and recommendations.

The results of the audit are based on our review of documentation and other information made available to us by CDFA and Sparboe Farms, Inc. During the three fiscal years under review, Sparboe Farms stated they had agreements with six vendors to pay the assessment fees for shell egg shipments to California. However, detailed fee payment records from the vendors were unavailable, or in one instance, the vendor stated it did not make any payments on behalf of Sparboe Farms. As a result, \$39,568 in fee payments could not be verified, as illustrated in Table 1.

**Table 1: Sparboe Farms—July 1, 2008 through June 30, 2011**

<b>Unverified Assessment Fee Payments</b>		
<b>Fiscal Year</b>	<b>Number of Cases</b>	<b>Assessment Fees</b>
2008-09	368,876	\$16,599
2009-10	350,749	\$ 1,754
2010-11	471,443	\$21,215
<b>Total</b>	<b>1,191,068</b>	<b>\$39,568</b>

CDFA has calculated and provided Finance with the applicable penalties and interest amount of \$47,523 for inclusion in this report. CDFA will issue a demand letter for the amounts due.

California Administrative Code, Title 3, Division 3, Chapter 1, Subchapter 3, section 1358, requires out-of-state egg producers to remit assessment fees to CDFA based upon the number of 30 dozen cases shipped to California.

Food and Agricultural Code section 27551 (c) requires out of state egg handlers and producers to report and pay the fee on egg sales into California sold to a retailer, producer, handler, or breaking plant, and on egg products brought into the state at a maximum rate of fifteen cents (\$0.15) for each equivalent of 30 dozen eggs.

**Recommendations:**

Remit \$87,091 (\$39,568 and \$47,523) in unverified assessment fee payments and applicable penalties and interest.

Ensure future assessment fee payments are paid per the requirements of the Food and Agricultural Code.





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July 19, 2013

Mr. David Botelho, CPA  
Chief, Office of State Audits and Evaluations  
California Department of Finance  
915 L Street  
Sacramento, CA 95814-3706

Response letter to draft report, Egg quality control mill fee assessment reports audit,  
Contract 12-0063.

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Dear Mr. Botelho:

Thank you for your letter dated May 7, 2013. We understand your request but respectfully disagree with the assessment.

Sparboe committed much time and resources to facilitating the audit team that visited our Corporate office. Every request they made was granted. All the reports and backup we provided were complete and thorough. We willingly provided all information to assist the auditors, but as a producer we face many challenges in the arena of egg taxes assessed to us when we don't always know where our eggs end up. In fact, the majority of the eggs we pay assessments on would probably not show under our name at the California border station, since they are typically shipped in by our customers. Despite that, we provided accurate reports that contained all the eggs we could identify which were shipped into the state of California.

With industry distribution channels that have changed over the years, it isn't always possible to know in which state our eggs land. We receive a written affirmation from our customers that commits them to making the payments. Sparboe provided those letters to the audit team. We understand the current law and are fully compliant today. For the egg taxes we paid, the audit team found no issues, as our payments and records were in order. The egg mill fee assessment laws have changed over the years and have been enforced differently than in the past. The attached letter from the Department of Agriculture dated June 25, 2012 suggests an effective date of July 1, 2012. The audit covered July 1, 2008 through June 30, 2011. Those changes prompted us to change the practice of having some of our customers pay the fee to California and we are now paying that directly.

Subsequent to the audit, Sparboe and the audit team worked together to contact our customers who committed to paying the egg taxes. Some of these customers buy eggs from other producers and don't necessarily segregate that on the reports submitted to California. The approach was to confirm that what they paid more than covered the fee that related to our egg volume. In most cases, this proved successful. I believe there was one small volume customer who admitted to the audit team they didn't pay the fee.



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Furthermore, the vast majority of the volume included in the fee assessment from your report is from our customers who don't own any birds or produce any eggs. Therefore, if you expect us to pay the assessed fee, our customers should not be required to pay any egg taxes and should be provided full refunds of all payments for all volume for all years paid. It is clear that, although your intent may not be to collect two fees on all dozens, that is what will happen if Sparboe pays the fees the report is requesting. Given that the fees our customers paid were in excess of our volume, California would stand to lose significant money.

Sparboe understands the need to conduct audits to verify reporting and compliance. We also appreciate the interaction with the audit team as we worked well together. We know there is a cost to conducting the audits and have paid the invoice for travel expenses for the audit. Sparboe complies with the laws as they are written. We believe it is unfair to attempt to collect double for the volume that was paid for by our customers.

We strongly believe the appropriate course of action would be to dismiss the charges based on the above mentioned facts.

Respectfully submitted,

Original signed by:

Craig Boesen  
Director of Accounting and Financial Reporting  
Sparboe Farms, Inc.  
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CC: Susan Botkin, Manager

## EVALUATION OF RESPONSE

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We reviewed Sparboe Farms' response, dated July 19, 2013, to our draft audit report. During our audit, we selected egg shipments only destined for California to examine mill fee assessments payable to CDFA. Additionally, the handlers responsible for the payment of fees for Sparboe egg shipments to California were unable to produce evidence the payments were made. As a result, our audit results are unchanged.