



State of Tennessee  
Department of Audit  
**2012 ANNUAL REPORT**

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Justin P. Wilson, Comptroller of the Treasury



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**Justin P. Wilson**

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**Justin P. Wilson**  
Comptroller

December 28, 2012

The Honorable Governor Bill Haslam  
The Honorable Ron Ramsey, Speaker of the Senate  
The Honorable Beth Harwell, Speaker of the House of Representatives, and  
Members of the General Assembly  
State Capitol  
Nashville, Tennessee 37243

Ladies and Gentlemen:

The 2012 annual report of the Department of Audit is submitted herewith in accordance with Section 4-3-304 of *Tennessee Code Annotated*.

The Department of Audit conducts audits or ensures that audits are conducted of state, county, and municipal governments; utility districts; internal school funds; and other local government authorities and agencies. Audits are also performed of state grants to nongovernmental organizations and of numerous federal programs for state and local governments.

In submitting this report, I would like to express my appreciation to all those who made possible the results reported, particularly the members of the General Assembly and the staff of this office.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Justin P. Wilson".

Justin P. Wilson  
Comptroller of the Treasury

JPW/ab



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# Department of Audit

## 2012 Annual Report

The General Assembly created the Department of Audit in 1937. Authority to audit state and county governmental entities is contained primarily in Section 4-3-304, *Tennessee Code Annotated*. The department is required to:

- perform currently a post-audit of all accounts and financial records of the state government . . . in accordance with generally accepted auditing standards and . . . such procedures as may be established by the comptroller . . .
- make annually, and at such other times as the general assembly shall require, a complete report on the post audit . . .
- certify to the fund balance sheets, operating and other statements, covering the condition of the state's finances, as prepared by the department of finance and administration, or by the state treasurer, before publication of such statements . . .
- serve as a staff agency to the general assembly, or to any of its committees, in making investigations of any phase of the state's finances . . .
- make annually an audit of all the records of the several counties of the state . . .
- perform economy and efficiency audits, program results audits and program evaluations . . .
- require that audits to be performed by the internal audit staffs of grantees or the internal audit staffs of state departments, boards, commissions, institutions, agencies, authorities or other entities of the state shall be coordinated with the office of the comptroller of the treasury . . . in accordance with standards established by the comptroller . . .
- require that all persons, corporations or other entities who receive grants from or through this state shall cause a timely audit to be performed, in accordance with auditing standards prescribed by the comptroller . . .

As of the year ended June 30, 2012, the Department of Audit comprises three divisions—State Audit, County Audit, and Municipal Audit—and employs approximately 300 people.\* Each division is administered by a director and is responsible for the audit function and addressing audit concerns and issues in the division. The Assistant to the Comptroller for the Department of Audit is responsible for overseeing department-wide activities and coordinating with the directors in carrying out the goals and objectives of each of the three audit divisions.

The Department of Audit is a post-audit agency. As such, it audits an entity's basic financial statements; an entity's compliance with applicable statutes, grant agreements, rules, and regulations; and/or its past record of efficiency and effectiveness at the end of a fiscal period.

Because independence is so important in a post-audit agency, the Department of Audit is in the legislative

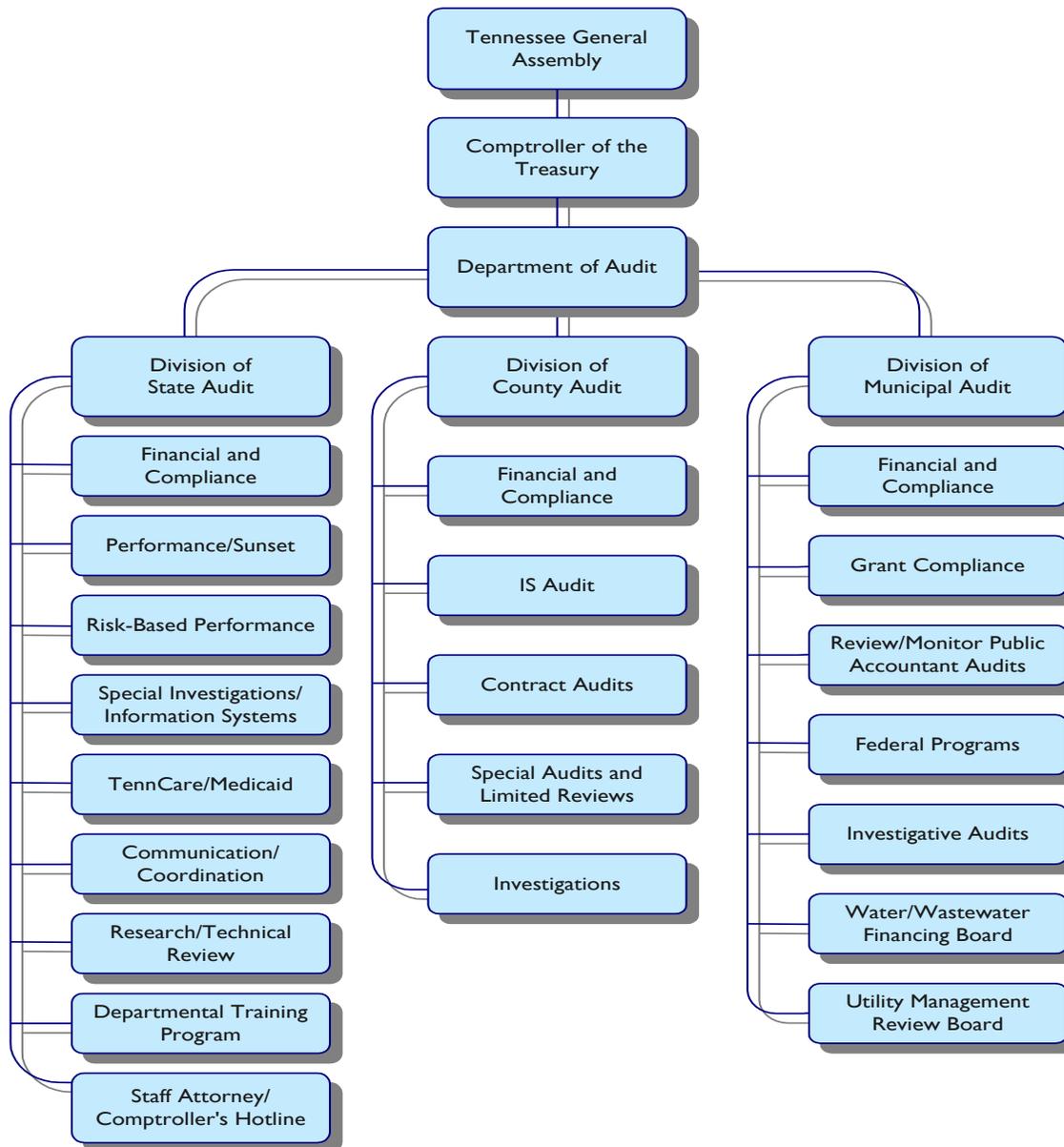
branch of state government. The department is accountable to the General Assembly and provides information to assist the legislature in overseeing the use of public funds and the efficient operation of government.

The basic purpose of post-audits is to identify and report material misstatements or noncompliance, whether due to fraud or errors, and recommend improvements. Pre-audits, in contrast, are performed by an entity's employees to prevent fraud and errors, detect problems, and suggest improvements. The most important distinction between the two is that post-audits are independent of the audited entity. In this respect, a post-audit agency in government is comparable to an independent certified public accounting firm in the private or business sector.

*\*(For information about the department's reorganization and structure, see page 3.)*

For additional information on the Department of Audit and the Comptroller, go to [www.comptroller.tn.gov](http://www.comptroller.tn.gov).

## Department of Audit Organizational Chart



### Auditing Standards

The Department of Audit performs audits in accordance with auditing standards generally accepted in the United States of America promulgated by the American Institute of Certified Public Accountants (AICPA) and generally accepted government auditing standards as set forth by the Comptroller General of the United States in *Government Auditing Standards* (Yellow Book).

These standards apply to financial and performance audits and attestation engagements. The Yellow Book

incorporates auditing standards generally accepted in the United States of America for field work and reporting and attestation standards promulgated by the AICPA.

The Department of Audit conducts its Single Audit in accordance with the Single Audit Act as amended by the 1996 Single Audit Act amendments and Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

## Peer Review

To comply with Section 8-4-102, *Tennessee Code Annotated*, the Speakers direct the Department of Audit to undergo a quality assessment review under the auspices of the National State Auditors Association. The most recent was performed in August 2012 by certified public accountants and other federal and state government professionals. The purpose of the review was to ensure that the department is following auditing standards generally accepted in the United States of America and standards contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

The peer review for the year ended June 30, 2012, rendered an unqualified opinion on the department's system of quality control. In the opinion of the quality assessment team, "the system of quality control of the State of Tennessee Comptroller of the Treasury, Department of Audit in effect for the period of July 1, 2011, through June 30, 2012, has been suitably designed and was complied with during the period to provide reasonable assurance of conforming with applicable auditing standards." The next review is scheduled for August 2014. □

## Department of Audit Reorganization

During the fiscal year ended June 30, 2012, the Department of Audit began a major reorganization of its structure.

The audit and contract review functions of the Divisions of County Audit and Municipal Audit were officially combined. With the merging of these functions, the Division of County Audit was renamed the **Division of Local Government Audit**.

The **Division of Investigations** was created in 2012 by consolidating the investigative groups of the divisions of State Audit, County Audit, and Municipal Audit. The consolidation created a unified team of highly skilled and uniquely talented investigators who bring expertise in various types of investigations. The Division investigates

allegations of fraud, waste, and abuse in state and local governments and other publicly funded entities within the State of Tennessee and reports the results of its investigations, including significant internal control and compliance deficiencies noted during the investigation. These investigations provide a basis, where applicable, for prosecutorial or administrative agencies to pursue criminal, civil, and/or administrative actions. Where criminal matters are involved, the Division works with the local District Attorneys General, the State Attorney General, TBI, FBI, and other federal, state, and local law enforcement.

These organizational changes will be reflected in the 2013 report.

## Department Reorganization





# Comptroller of the Treasury Strategic Plan Framework



## *Mission*

**To improve the quality of life for all Tennesseans  
by making government work better**

## *Purpose*

**To serve the people of Tennessee by:**

- Contributing to the protection of the public trust and promoting the public interest
- Enhancing effective public policy decisions at all levels of government
- Fulfilling operational and oversight responsibilities as may be assigned with the highest possible degree of excellence, efficiency, and effectiveness

## *Goals and Objectives*

**Assure public resources are used effectively, efficiently,  
and in compliance with applicable law**

- Exercise an oversight role of governmental entities and agencies
- Continue to evaluate the effectiveness and efficiency of resources used by each division through a performance-based operation
- Ensure the secure, efficient, and effective use of technology solutions

**Accomplish and provide continuous improvement for the statutory  
and other assigned responsibilities of the Comptroller's Office**

- Use cross-divisional teams to address office-wide themes and appropriate strategic objectives
- Continue to advance the Comptroller's Office to a performance-based operation

**Provide timely, adequate, and accurate information to decision makers at all government levels**

- Maintain a process to develop appropriate information for decision makers
- Maintain a process to provide decision makers with appropriate information concerning policy, resource use, and management
- Encourage cooperation and joint efforts among divisions

**Provide a diverse, competent, ethical and professional staff  
and maintain continual development of such staff**

- Adhere to a uniform Code of Ethics Program
- Maintain a succession plan for management
- Maintain a training program for the continual development of all staff
- Seek a healthy and safe work environment
- Review compensation issues within the Comptroller's Office on an annual basis
- Maintain a recruiting and hiring process that promotes diversity

**Provide and maintain effective communication with internal and external audiences**

- Maintain and improve a program which coordinates timely communications using the best available technology for internal and external communications
- Maintain appropriate historical information
- Inform and educate the citizens of the state, the general assembly, and other government entities about the role of the Comptroller
- Maintain a pro-active presence in professional organizations and associations

## *Core Values*

<i>Honesty and Integrity</i>	<i>Accuracy and Reliability</i>	<i>Accountability</i>
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# Division of State Audit

The Division of State Audit conducts financial and compliance audits, performance audits, and investigations. It also performs special studies to provide the General Assembly, the Governor, and the citizens of Tennessee with objective information about the state's financial condition and the performance of the state's agencies and programs. This division thus aids the legislature in ensuring that state government is accountable to the citizens of Tennessee. In fulfilling this audit function, the division issued 58 reports during the year ended June 30, 2012; an additional 101 audits and special investigations were in progress at June 30, 2012.

This division includes six sections: Financial and Compliance, Performance (Sunset), Risk-Based Performance, TennCare, Special Investigations, and Information Systems. Highlights of work from July 1, 2011, through June 30, 2012, are presented. Complete reports are available at [www.comptroller.tn.gov/sa/AuditReportCategories.asp](http://www.comptroller.tn.gov/sa/AuditReportCategories.asp).

In addition to auditing, the division reviews and comments on due process documents from professional organizations and conducts technical research and training. The division also assists the Comptroller in the formulation of state policy and regulations, either directly by consulting with representatives of state agencies or indirectly by submitting comments about proposed policies and procedures.

## Financial and Compliance

The Financial and Compliance section conducts financial and compliance audits of state departments, agencies, and institutions.

A major endeavor of the Financial and Compliance section was the Single Audit of the State of Tennessee for the year ended June 30, 2011, conducted in accordance with Office of Management and Budget (OMB) Circular A-133. The *Single Audit Report* reflected federal awards of over \$16.9 billion.

We noted instances of noncompliance that resulted in qualified opinions on compliance for 6 of the state's 32 major federal programs. In addition, we noted other instances of noncompliance that met the reporting criteria contained in OMB Circular A-133. We also noted material weaknesses and significant deficiencies in internal control over compliance with requirements related to federal programs.

As a result of testing the state's compliance with the requirements of laws, regulations, contracts, and grant agreements applicable to each major federal program, costs of \$1,663,785.96 were questioned. We noted two deficiencies that we considered to be material weaknesses in internal control over financial reporting. We noted no instances of noncompliance that we considered material to the state's basic financial statements.

The Single Audit included an audit of the state's basic financial statements. This audit resulted in an unqualified opinion on the basic financial statements of the State of Tennessee for the year ended June 30, 2011.

The audit also determined that the Schedule of Expenditures of Federal Awards was fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

In addition to the *Single Audit Report*, separate audit reports were issued on many agencies and institutions of state government including the Department of the Treasury, the Tennessee Consolidated Retirement System, state universities, the Tennessee State School Bond Authority, the Tennessee Local Development Authority, the Tennessee State Veterans' Homes Board, and the Tennessee Housing Development Agency.

The separate audits of the departments, agencies, and institutions are not meant to serve as organization-wide audits as described in the Single Audit Act as amended in 1996 and OMB Circular A-133. Some, however, serve as segments of the organization-wide audit of the State of Tennessee; therefore, they include the necessary tests for compliance with applicable laws, regulations, contracts, and grant agreements and the required consideration of the internal control.

## Audit Process

Financial and compliance audits are conducted in accordance with auditing standards generally accepted in the United States of America and generally accepted government auditing standards issued by the United States Comptroller General. The objectives of financial and compliance audits are

- to consider the entity's internal control over financial reporting as a basis for designing auditing procedures to express an opinion on the financial statements;
- to determine compliance with certain provisions of laws, regulations, contracts, and grant agreements;
- to determine the fairness of the presentation of the financial statements; and
- to recommend appropriate actions to correct deficiencies.

## Results of Audits

During the year ended June 30, 2012, the division published 33 financial and compliance audit reports containing 47 audit findings and issued opinions on 46 sets of financial statements. On June 30, 2012, another 43 audits were in progress. The section released financial and compliance audit reports for the following entities:

- ◇ Chattanooga State Community College
- ◇ Chattanooga State Technical Community College Foundation
- ◇ Clean Water State Revolving Fund
- ◇ Cleveland State Community College
- ◇ Columbia State Community College
- ◇ Comprehensive Annual Financial Report
- ◇ Department of the Treasury
- ◇ Dyersburg State Community College
- ◇ East Tennessee State University
- ◇ Endowment for Educational Excellence: Tennessee State University Foundation
- ◇ Middle Tennessee State University
- ◇ Motlow State Community College
- ◇ Single Audit for the State of Tennessee
- ◇ Southwest Tennessee Community College
- ◇ Tennessee Board of Regents State University and Community College System of Tennessee – Central Office
- ◇ Tennessee Consolidated Retirement System
- ◇ Tennessee Education Lottery Corporation
- ◇ Tennessee Housing Development Agency
- ◇ Tennessee Local Development Authority
- ◇ Tennessee Residence Foundation 2010, 2011

- ◇ Tennessee Sports Hall of Fame
- ◇ Tennessee State School Bond Authority 2010, 2011
- ◇ Tennessee State University
- ◇ Tennessee State Veterans' Homes Board
- ◇ Tennessee Student Assistance Corporation 2010, 2011
- ◇ Tennessee Technological University 2010, 2011
- ◇ The University of Memphis
- ◇ The University of Tennessee
- ◇ Volunteer State Community College

## Special Investigations

The Special Investigations section gathers information and evidence resulting in prosecutions and recovery of funds and coordinates the efforts of other agencies in the investigation, with authority provided in part by Sections 8-4-201 through 8-4-208, *Tennessee Code Annotated*. The investigators assist local district attorneys general, Tennessee's Office of the Attorney General, the Office of the United States Attorney General, and the Tennessee Bureau of Investigation.

Investigative reviews are initiated as a result of information from the Department of Audit, individuals, other departments and agencies, or the Comptroller's hotline answered by staff of the section.

For the year ended June 30, 2012, the section received a total of 343 notifications of possible fraud, waste, or abuse. At the beginning of the year, the section had 14 active cases. During the year, the section opened three cases and closed eight cases, with an outstanding balance of nine cases at year-end. Investigations were completed on matters at the state as well as local level. Matters investigated ranged from alleged embezzlement of public funds to alleged abuse of public resources. One report was released:

- ◇ Tennessee Wildlife Resources Agency – Theft of Pay Lake Funds

Investigators found that weak internal controls or ineffective management were contributing factors in most of the losses incurred as a result of fraud. When investigators find such weaknesses, they share the information with State Audit financial auditors for consideration in audits of the affected entity.

## Performance

A performance audit is an independent examination of the extent to which agencies and departments of state government are faithfully carrying out their programs. The audit reports assist the General Assembly and agency management by

- assessing the extent to which state agencies have fulfilled their statutory mandate and the efficiency and effectiveness of their organization and use of resources,
- developing recommendations for management or legislative action that might improve the efficiency and effectiveness of the agencies' operations, and
- providing program and financial data.

Most of the Performance Audit section's workload is directed by the Tennessee Governmental Entity Review Law, known as the Sunset Law (Section 4-29-101 et seq., *Tennessee Code Annotated*), which requires the Joint Government Operations Committee to review each entity at least once every eight years to determine whether the entity should be continued, restructured, or terminated.

Other performance audit work is based on risk assessment of state department and agency programs. The risk-based performance audit group conducts audits based on identification of risks in state-wide processes and programs and agency-specific operations and activities. During FY2012, with increased federal funding and new reporting requirements under the American Recovery and Reinvestment Act of 2009, state agencies were at greater risk of fraud, waste, abuse, and noncompliance with federal program requirements. The risk-based performance audit group performed audits of those state agencies with the greatest risks.

Audit staff focus on audits of major entities. In the year ended June 30, 2012, the Performance Audit section released the following 10 reports:

### Sunset Audit Reports

- ◇ Board for Licensing Health Care Facilities and Division of Health Care Facilities
- ◇ Department of Environment and Conservation and Related Environmental Boards
- ◇ Department of General Services
- ◇ Department of Human Services
- ◇ Tennessee Emergency Management Agency and Related Compacts

### Special Reports

- ◇ Annual Report on the Status of Submission of Title IX Implementation Plans

- ◇ Implementation of the Complete College Tennessee Act of 2010
- ◇ Issues Regarding the Efficiency, Effectiveness, and Fairness of Hiring and Promoting Individuals Through the State of Tennessee's Current Civil Service Process
- ◇ Office of the Comptroller of the Treasury
- ◇ Review of Tennessee's Contract Monitoring and Management Systems

Thirty engagements were in process at year-end.

The Government Operations Committees held 13 public hearings on 68 entities in the year ended June 30, 2012. At these hearings, Performance Audit staff presented audit reports covering 13 entities. Another 46 entities submitted written responses to staff-prepared questions based on the entities' statutory authority and responsibility. Additionally, the committees held procedural hearings on self-sufficiency issues on eight entities and a follow-up hearing on one entity.

## Audit Process

Performance audits are conducted in accordance with *Government Auditing Standards* issued by the United States Comptroller General and move through six phases: planning, fieldwork, report writing, agency comments, report publication, and presentation at a legislative hearing. Performance audits include the following:

- Review of relevant laws, cases, Attorney General's opinions, executive orders, rules, and regulations.
- Review of the agency's procedures, plans, and records.
- Interviews with staff of the agency and related agencies.
- Observation of the agency's operations and activities.
- Analysis of the agency's revenue and expenditure data, program data, performance, and results.
- Review of comparative data from other states.
- Surveys of individuals, agencies, and organizations served or affected by the agency.
- Tests for compliance with legal requirements.
- Evaluation of the extent to which the agency achieved desired results at the lowest reasonable cost.
- Legislative or administrative recommendations for accomplishing the agency's legislative mandate.

## TennCare

The TennCare section of the Division of State Audit, under an agreement with the Department of Finance and Administration, performs certain audit and rate-setting functions for the state's TennCare program. A staff of 22 professional auditors performs the following functions:

- Reimbursable rate computation and examinations for nursing homes and Intermediate Care Mental Retardation facilities participating in the Medicaid Program.
- Computing of reimbursement settlements and prospective rates for Federally Qualified Health Centers and Rural Health Clinics as required by the Benefits Improvement and Protection Act of 2000.
- Cost settlements for state-operated Development Centers serving mentally retarded recipients.
- Provide financial and budgeting support to the Bureau from nursing home paid claims extracts.
- Examinations of TennCare Managed Care Contractors (MCCs) contracting with the state to provide medical services under the program, performed jointly with the Department of Commerce and Insurance.

### Examinations of Nursing Facilities

In the fiscal year ended June 30, 2012, the TennCare section completed 15 examinations of the following nursing facilities:

- ◇ Americare Long Term Specialty Hospital
- ◇ Lincoln and Donalson Care Centers
- ◇ Raintree Manor
- ◇ Countryside Healthcare and Rehabilitation
- ◇ The Bridge at South Pittsburg
- ◇ Life Care Center of Tullahoma
- ◇ Henry County Healthcare Center
- ◇ The Bridge at Monteagle
- ◇ Summit View of Lake City
- ◇ Life Care Center of Morristown
- ◇ Life Care Center of Cleveland
- ◇ Green Hills Health and Rehabilitation Center
- ◇ Etowah Health Care Center
- ◇ Buffalo River Health Center, d/b/a Perry County
- ◇ Signature Healthcare of Saint Francis

Sixteen examinations were in progress at year-end.

## Information Systems

The Information Systems (IS) section provides three basic services: data retrieval, IS systems review, and computer forensic analysis.

To provide information for audit fieldwork, the data retrieval staff write computer programs to provide information from the state's centralized accounting system, individual agency service delivery systems, and college and university transaction files.

The IS review staff are responsible for obtaining and documenting an understanding of internal control in the computerized accounting and management information systems of entities undergoing audits by other sections of the division. Three audits were in progress at June 30, 2012.

The IS section provides services in the area of computer forensic analysis. Evidence of fraud and abuse may be found on subjects' computers, and the IS section works in support of the special investigations section to acquire, identify, and analyze this evidence. The section utilizes specialized software and hardware to recover evidence of official misconduct by state employees and in support of civil or criminal action against persons or entities engaging in illegal activities resulting in damages to the state.

### Examinations of TennCare MCCs

In the fiscal year ended June 30, 2012, the TennCare section assisted the Department of Commerce and Insurance in two Managed Care Contractor (MCC) examinations. The summary of findings included financial, claims processing, and compliance deficiencies.

### Special Projects – Grier Consent Decree

The state, legislature, or federal government often requests that the Division of State Audit work on special TennCare projects. In one such project, the state, under a consent decree with the federal court, has agreed to comply with requirements with respect to TennCare enrollee grievances and appeals. The TennCare managed care contractors and providers are also subject to the decree, so it has widespread implications.

The agreement, commonly referred to as the "Grier Consent Decree," became effective November 1, 2000. The decree requires the state to enter into an agreement with the Comptroller's Office to monitor compliance and to report quarterly. Reports through the end of 2011 have been completed, and reports for 2012 are in progress. □



# Division of County Audit

The Department of Audit, through the Division of County Audit, is responsible for the annual audits of all 95 counties in the state. The division may conduct the audit of a county or accept an audit prepared by a certified public accountant provided the audit meets minimum standards for county audits established by the Comptroller of the Treasury. However, the Division of County Audit is required to prepare an audit in each county at least once every five years or to participate with, or monitor the audit with, the certified public accountant.

## Financial and Compliance

The division presently conducts audits in 89 counties. These audits are assigned to teams that audit the various offices and/or departments and entities of county government. The audit staff is divided into four geographical areas: East, Mideast, Middle, and West. Each area is under the supervision of an audit manager who is responsible for audit planning and supervision.

## The Audit Process

The Division of County Audit performs the following general procedures as part of the financial and compliance audit process:

- Evaluates the entity's existing internal controls in the appropriate areas of operation.
- Confirms the accountability for receipts by examining, for example, tax rolls, state and federal revenue data, and letters of inquiry.
- Determines the appropriateness of disbursements by examining budget authorization, paid invoice files, purchasing files, payroll records, and other financial records.
- Determines the authorization for transactions by reviewing the minutes of meetings of county commissions, school boards, highway commissions, and various committees such as budget and finance, and purchasing.
- Determines compliance with federal regulations and state and local laws.
- Obtains management's representations with respect to the financial statements, as well as the supporting accounting data, and other items of disclosure.

- Evaluates financial statement presentation to determine conformity with accounting principles generally accepted in the United States of America.
- Evaluates the validity of all evidence obtained throughout the audit process to formulate an opinion on the financial statements.

## Scope of Activity

### Post-Audit of County Governments

The Division of County Audit conducted audits in 89 of the state's 95 counties for the 2010-2011 audit year. A minimum of ten offices or departments in each county was audited:

1. County Trustee
2. County Mayor
3. Department of Education
4. Department of Highways
5. County Clerk
6. Circuit Court Clerk
7. General Sessions Court Clerk
8. Chancery Court Clerk and Master
9. Register
10. Sheriff

The audits of all offices were for the fiscal year ended June 30, 2011. The audit field work in each county is conducted by an audit team. The size of the team is determined by the complexity of the assignment. Approximately ten weeks of field work are required, including audit review and supervision by an auditor 4 and/or audit manager. The draft audit reports are reviewed in the Nashville office and released. The division also prepares audits of two special school districts and performs special audits and reviews as requested or as deemed necessary.

## Results of Audits

### Financial and Compliance Audits

Audits of financial transactions for the fiscal year ended June 30, 2011, conducted by the Division of County Audit disclosed cash shortages in the following offices or funds:

The audits conducted or reviewed by this division disclosed fund deficits totaling \$110,293,520 in 17 governmental fund accounts in 14 counties. Audits also reflected net asset deficits totaling \$83,243,922 in 17 enterprise funds and 6 internal service fund accounts in 14 counties. Details of the latest cash shortages report are available on the Comptroller's website at [www.comptroller.tn.gov](http://www.comptroller.tn.gov).

### Information System Reviews

Most county government offices and departments in Tennessee have automated all or a portion of their daily operations. The information system (IS) review section is responsible for evaluating those computer-based accounting and information systems to determine whether an entity's existing procedures and controls provide adequate assurance of data accuracy and financial and operating statement reliability. An assistant director supervises this section's IS audit manager and seven IS auditors, who are assigned to different areas of the state.

General and application controls of a county's computer hardware and computerized accounting and information systems are evaluated. Findings resulting from this evaluation are discussed with the appropriate officials and included in the county's annual financial report.

#### Scope of Activity

##### Information System Reviews

As required by the division's annual audit plan, information system related controls were evaluated in 89 counties and two special school districts during the year ending June 30, 2012.

### Contract Audits

For six counties, certified public accountants perform the financial and compliance audits. The division monitors these audits in accordance with a four-year monitoring plan, which includes a review of working papers prepared by certified public accountants.

The division also approves the contracts of certified public accountants and reviews their audit reports and working

papers. The objective of this review is to ensure that in addition to the standards prescribed by the American Institute of Certified Public Accountants and Government Auditing Standards issued by the United States Comptroller General, certain standards prescribed by the Comptroller of the Treasury have been followed.

#### Scope of Activity

##### Monitoring and Review of Contract Audits

The division will monitor audits of six county governments during the next four years. The audits of Washington, Shelby, and McMinn counties will be monitored for the year ended June 30, 2012.

The division reviewed 285 audit reports for the year ended June 30, 2011, submitted by certified public accountants for audits of county governments, authorities, boards, commissions, agencies, and special school districts. The division anticipates it will review 289 such reports for the year ended June 30, 2012.



## Investigations

A County Audit investigations team performs investigations on reported instances of fraud, waste, and abuse. The team consists of four auditors, one based out of each of the division's regional offices. An investigations manager sets priorities, allocates resources, and coordinates investigations with area audit managers. The investigative auditors' primary responsibility is to perform investigations in their geographic area resulting from hot line calls, fraud reporting forms, anonymous tips, significant cash shortages discovered during the routine audit process, and other reported instances of fraud, waste, and abuse. Results of investigations, such as findings and any impact on county financial statements, will be reported in the annual county audit reports. On occasion, a separate investigative report may be issued.

In most cases, investigative auditors discovered weak internal controls or ineffective management that created an environment where fraud could occur and go undetected. During the fiscal year ended June 30, 2012, the division released eight special investigative reports revealing a loss of county funds to fraud totaling \$240,691.43. The following special reports were released in the fiscal year June 30, 2012:

- ◆ 24th Judicial District
- ◆ Davidson County Trustee
- ◆ Davidson County Clerk
- ◆ Cannon County REACH After-School Program
- ◆ Morgan County Soil Conservation District
- ◆ Millard Oakley Public Library
- ◆ Wilson County Joint Violent Crimes Taskforce and Safe Streets Task Force
- ◆ Warren County Memorial Airport

## Other Services

### Technical Assistance

In addition to the basic audit function and the monitoring and review of audits by certified public accountants, the division provides other services. These services include providing information and assistance to facilitate implementation of new auditing and accounting standards; submission of federal program data to the federal clearing house on behalf of county governments; requesting technical data for pension and other postemployment benefits note disclosures from the State of Tennessee; maintenance of the uniform chart of accounts used by county governments; and participation in the review of

telephone calls made to the Comptroller's Fraud Hotline. The division also provides, upon request, assistance to counties in resolving current problems with financial administration, as well as answering questions on various local governmental matters. The division provides fiscal reviews of new legislation related to county governments and works closely with the state legislature with regard to the passage of new statutes for county governments.

### Reviews of Funds Administered by District Attorneys General

During 2011, the division conducted reviews of District Attorney General Funds, Judicial District Drug Task Force Funds, and other funds the district attorneys general administer in the state's 31 judicial districts. Each review covered the period July 1, 2010, through June 30, 2011. The scope of each review was limited to the transactions of the individual funds and did not include the overall operation of the district attorneys' offices.

### Reviews of County Correctional Incentive Program (CCIP)

*Tennessee Code Annotated*, Title 41, Chapter 8, referred to as the County Correctional Incentive Act, provides counties financial incentives to house nondangerous felony offenders at local correctional facilities. The purpose of the program is to mutually benefit state and county governments by helping to alleviate overcrowding in state correctional facilities and reduce high operating costs, and to assist counties in upgrading local correctional facilities and programs. Counties participating in the program may be reimbursed at either a minimum statutory daily rate or a rate based on a county's "reasonable allowable cost" to house convicted felons.

The Division of County Audit conducts reviews of various counties participating in the CCIP. The objectives of the reviews were 1) to determine if prisoners were properly listed on the State Prisoner Reports, 2) to determine if inmates were accurately reported on the Correction Facility Summary Reports, and 3) to recommend appropriate actions to correct any deficiencies.

Reviews were conducted in 25 detention facilities for the year ended June 30, 2010. As a result of the reviews, it was determined that the state had overpaid \$61,145 for three facilities and underpaid \$58,232 for two facilities.

Reviews were conducted in 23 detention facilities for the year ended June 30, 2011. As a result of the reviews, it was determined that the state had overpaid \$4,480 for two facilities. □



# Division of Municipal Audit

The Division of Municipal Audit ensures that annual audits required by state statute, regulations, or contractual agreement are performed for Tennessee municipalities, public internal school funds, certain quasi governmental entities, utility districts, housing authorities, charter schools, and certain nonprofit and for profit organizations receiving funds from the State of Tennessee that are subject to audit by the Comptroller's Office. In addition, the division investigates allegations of misconduct, fraud, waste, and abuse in these entities.

## Audit Review Process

The Division fulfills its audit responsibility through a contractual process with independent certified public accountants who perform the audits for Tennessee's 343 municipalities and 104 municipal-related entities, 140 quasi governmental entities, 183 utility districts, 142 public internal school funds, 46 charter schools, 85 housing authorities, 3 housing authority related entities, and 326 nonprofit and for profit organizations. The entities use standard contracts, prepared by the Comptroller of the Treasury, which must be approved by the Comptroller's designee in the Division of Municipal Audit before audit work begins. These audits must be performed in accordance with generally accepted government auditing standards and certain other minimum requirements prescribed by the Comptroller of the Treasury. In addition, the auditor must comply with other federal and state provisions.

The Division of Municipal Audit reviews each audit report to verify that it adheres to applicable reporting requirements. If a local governmental unit fails or refuses to have an audit, the Comptroller may direct the Division of Municipal Audit, or may appoint a certified public accountant, to perform the audit. If a nonprofit or for profit organization refuses to have an audit, the Division works in connection with the respective state funding agency to obtain an audit. The division evaluates the audit working papers of certified public accounting firms that audit the entities. If the firm's audit working papers are deemed substandard, the Comptroller of the Treasury takes appropriate action, which might include referral to the State Board of Accountancy.

## Statutory Referral of Utility Systems

Sections 68-221-1010(a) and 7-82-703(a), *Tennessee Code Annotated*, require the Comptroller to refer financially distressed municipal water and/or wastewater

systems and public utility districts to the state's Water and Wastewater Financing Board and/or the Utility Management Review Board. Sections 68-221-1010(d) and 78-82-401(h) of *Tennessee Code Annotated* require the Comptroller to refer water systems with excessive unaccounted for water losses. After the Division of Municipal Audit refers applicable facilities to the appropriate board, the respective board obtains and reviews a proposed plan for correction by the facility. If the board finds the facility's plan unacceptable, the board will recommend an alternate course of action.

During the year ended June 30, 2012, 148 water and/or wastewater facilities were referred to the Water and Wastewater Financing Board, and 62 utility districts were referred to the Utility Management Review Board. As a result, several utility districts and municipal water and/or sewer systems are now operating or are on their way to operating on a financially sound basis and/or are in the process of taking measures to decrease their water loss rates.

## Investigative Audits

The division investigates allegations of misconduct, fraud, and waste in specified local governments and other publicly funded entities. Investigative audits are performed as a result of allegations received through the Department of Audit's toll-free hotline, routine audit reviews, information received from certified public accountants, other state agencies, concerned citizens and/or officials, and requests received from local district attorney generals, the State Attorney General's Office, the FBI, and other prosecutorial and law enforcement agencies. Upon completion of each examination, the Comptroller issues a report or letter presenting documented occurrences of improper activity and recommending corrective action. The report is forwarded to the State Attorney General and the local district attorney general for any legal action deemed necessary.

The division's investigative audits also include an assessment of internal controls and compliance with applicable laws relative to the issues investigated. Municipalities are required by statute to maintain their records, at a minimum level, in accordance with the *Internal Control and Compliance Manual for Tennessee Municipalities*, prescribed by the Comptroller of the Treasury. Utility districts are required by state statute to follow the *Uniform Accounting Manual for Tennessee Utility Districts*, compiled by the Division of Municipal Audit. State statute requires schools to follow the *Tennessee Internal School Uniform Accounting Policy Manual*, compiled by the Tennessee Department of Education, the Department of Finance and Administration, and the Comptroller of the Treasury. At the conclusion of an investigative audit, the division publishes a report that identifies internal control and compliance weaknesses and recommends corrective action. The audits point out to officials the importance of

sound internal controls and compliance with applicable laws and regulations.

The division routinely provides technical assistance to local government officials and certified public accountants. This assistance often requires detailed research of financial accounting concepts and state and federal statutes. □



## Audits and Investigative Audits

For the year ended June 30, 2012, the Division of Municipal Audit performed 1,472 reviews of audit reports for specified local governments and other publicly funded entities. The division released 23 investigative audits during the year. The entities examined in the 23 investigative audits included 10 municipalities, 6 public schools, 1 nonprofit entity, 1 utility district, and 5 school support organizations. Seven of the investigative audits uncovered fraud, waste, and abuse. Most investigative audits revealed weaknesses in internal controls, absence of internal controls, or potential problem areas that created an environment conducive to fraud. During the 2012 fiscal year, investigative audits revealed losses of at least \$374,861 due to fraud. In total, approximately 7 defendants' cases were disposed of in fiscal year 2012.

The Division of Municipal Audit released the following investigative audit reports during the year ended June 30, 2012:

- ◇ Community Health Network
- ◇ Riverdale High School Quarterback Club-Rutherford County Schools
- ◇ Caryville Elementary School-Campbell County Schools
- ◇ Town of Oakland
- ◇ City of Whitwell
- ◇ Ripley High School Lady Tigers Softball Booster Club
- ◇ Pigeon Forge Middle and High School Cheer Leaders-Sevier County Schools
- ◇ City of South Pittsburg
- ◇ City of Gallaway
- ◇ Town of Huntingdon
- ◇ Hillsboro High School Athletic Boosters (PTSA)-Metro-Nashville Public Schools
- ◇ City of Winchester
- ◇ Oak Ridge Utility District
- ◇ Tellico Plains Police Department
- ◇ McMinn Central Dance Team Booster Club-McMinn County Schools
- ◇ City of Collinwood
- ◇ Crump Police Department
- ◇ Nolachuckey Elementary School-Greene County Schools
- ◇ City of Jellico
- ◇ Valley Forge Elementary School-Carter County Schools
- ◇ Warren County High School Pioneer Band Boosters-Warren County Schools
- ◇ Warren County High School-Warren County Schools
- ◇ Smyrna Elementary School-Rutherford County Schools



# Comptroller's Hotline

Since its inception, the hotline has received over 16,000 calls, including 1,302 calls between July 1, 2011, and June 30, 2012. Of the 1,302 calls, 440 concerned allegations of fraud, waste, or abuse. The substantive calls—those relating to fraud, waste, or abuse—concerned a wide range of entities, including municipalities, counties, state agencies and departments, and federal agencies and departments. A more detailed analysis is below. Substantive calls are investigated by the Department of Audit or referred to the appropriate agency or program.

Of the 440 calls referred for action, responses have been received on 297, and these are considered closed. The remaining 143 continue to be considered open.

The remaining 862 calls have not been acted on because they were either repeat calls or were not relevant to the purpose of the hotline. Calls in the latter group include wrong numbers, hang-ups, general inquiries about the hotline, and requests for services provided by other agencies, such as tax assistance. Where applicable, the callers are referred to the appropriate agency or department that can provide assistance.

## Results of Hotline Calls

The following summaries are the results of hotline calls upon which corrective action was taken for the year ending June 30, 2012.

### Correction – Improper Use of Prison Labor

The caller alleged a correctional facility employee was utilizing an inmate to help file personal legal appeals. The allegation was found to be true, and the employee was suspended for five days.

### Correction – Inmate Prescriptions

The caller alleged that a correctional facility inmate was not receiving prescribed medication timely. The department identified the problem and implemented measures to prevent recurrence of the issue.

### Health – Unprofessional Behavior

The caller alleged that a health department employee would not let the caller accompany the caller's non-English-speaking spouse during a medical visit. The review determined that the health department employee should have confirmed with the spouse to allow the caller's presence. A corrective action plan was initiated.

### Health – Refusal to Provide Services

The caller alleged that a health department would not give the caller's child a tetanus shot due to the caller being insured. It was determined that the staff had misinterpreted the Department of Health's policy regarding immunizations. The Director of the Immunization Program met with staff and explained that

the caller's child was eligible for a tetanus shot.

### Human Services – Unsafe Day-Care Practices (Two Cases)

In one instance, a caller alleged that a day-care facility transport van's tags had expired. The allegation was found to be true, and the center voluntarily suspended transportation services. In another instance, a caller alleged that a day-care was not complying with supervision ratios. The allegation was found to be true, and it was discovered that the center had not kept proper staff attendance records. The center was issued a warning and was required to correct the violations.

### Human Services – Food Stamp Fraud (Seven Cases)

In all instances, a caller alleged an individual was receiving food stamp benefits for which that individual was not eligible, and the allegation was found to be true. In four of those instances, the recipient had failed to update a change in household composition and the department reduced the recipient's benefits. And in one instance where the recipient had unreported income, the individual retained a reduced benefit and the department is seeking recovery for the months in question.

### Human Services – Unprofessional Behavior

It was alleged that the caller had to wait an unreasonable amount of time for a telephone interview. It was determined that the caller was not called during the scheduled time. Procedures were implemented to call a client if the scheduled time cannot be met.

### **Human Services – Caseworker Not Following Court Order**

The caller alleged that a caseworker was not following the steps necessary to establish paternity and set support for the caller's case. The review determined that timely action had not been taken. A court date was set to establish paternity and set a support amount.

### **Human Services – Improper Charge for Child Support**

It was alleged that the caller was being charged for child support while the custodial parent and child resided with the caller. It was determined that the caller should not have been charged for child support during this period. The department adjusted the amount owed by \$1,180.00.

### **Labor – Failure to Pay Workers' Compensation**

The caller alleged that a company had failed to maintain workers' compensation insurance coverage. The allegation was found to be true. The department assessed the company a penalty of \$4,047.97.

### **Labor – Unemployment Fraud**

The caller alleged that an individual was receiving unemployment compensation while the individual was ineligible to do so due to being employed. The allegation was found to be true, and the department established a fraud overpayment of \$5,464.00.

### **Mental Health and Substance Abuse Services – Unprofessional Behavior**

The caller alleged that an employee of a treatment facility allowed another individual to receive services before the caller, although the caller was next on the waiting list. The allegation was found to be true. The employee no longer has the responsibility for designating the order in which individuals receive needed services.

### **Safety – Unprofessional Behavior (Four Calls)**

In all instances, the callers alleged that that they were treated unprofessionally at driver's license testing stations. In three instances, the review determined that the station had failed to follow procedures outlined by the department for the issuance or reissuance of licenses. In the other instance, an employee was warned for making personal calls during work hours.

### **Transportation – Unprofessional Behavior Transportation Services (Four Calls)**

In all instances, the callers alleged that drivers for public transportation services had acted unprofessionally. In one instance, the caller alleged a driver was talking on a cell phone while operating a vehicle. It was determined that the caller was violating agency policy and was required to receive additional training/counseling. In another instance, the caller alleged that a driver was smoking in an agency vehicle. The allegation was found



to be true, and the employee was terminated. Another caller alleged that a director of an agency that provides transportation services allowed a family member to receive services in violation of agency policy. The allegation was found to be true, and the director was reprimanded and is now required to receive exception approvals from the Transportation Program Director. In the last instance, the caller alleged that transportation services had left the caller stranded at the caller's doctor's office for over five hours. The allegation was found to be true and was attributed to miscommunication between the transportation service manager and drivers. The manager and drivers were required to take additional training.

### **Transportation – Time and Attendance**

The caller alleged that an employee was falsifying time and attendance sheets. The allegation was substantiated for a total amount of \$2,424.25. The employee retired from state service, and the employee's supervisor was issued a written warning for failing to properly supervise. □

**Analysis of Substantive Hotline Calls**  
**Fiscal Year Ended June 30, 2012**

<b>Reviewing Agency</b>	<b>Calls</b>	<b>Closed</b>	<b>Open</b>
<u>State Government</u>			
Agriculture	1	0	1
Board of Probation and Parole	3	2	1
Board of Regents	7	2	5
Children's Services	9	3	6
Commerce and Insurance	3	2	1
Comptroller	167	84	83
Correction	5	3	2
Corrections Institute	4	4	0
Environment and Conservation	6	6	0
General Services	2	0	2
Health	46	43	3
Human Services	72	66	6
Intellectual and Developmental Disabilities	9	1	8
Labor	12	7	5
Mental Health	12	10	2
Revenue	2	2	0
Safety	20	15	5
TennCare	7	5	2
Tennessee Housing Development	1	0	1
Transportation	39	34	5
University of Tennessee	1	1	0
Veterans' Affairs	1	0	1
<u>Federal Government</u>			
Head Start	1	0	1
Housing and Urban Development	7	5	2
Social Security	3	2	1
<b>Total</b>	<b>440</b>	<b>297</b>	<b>143</b>

Comptroller's Fraud, Waste, and Abuse Hotline  
**(800) 232-5454**



# About the Department of Audit

## Department of Audit Staff

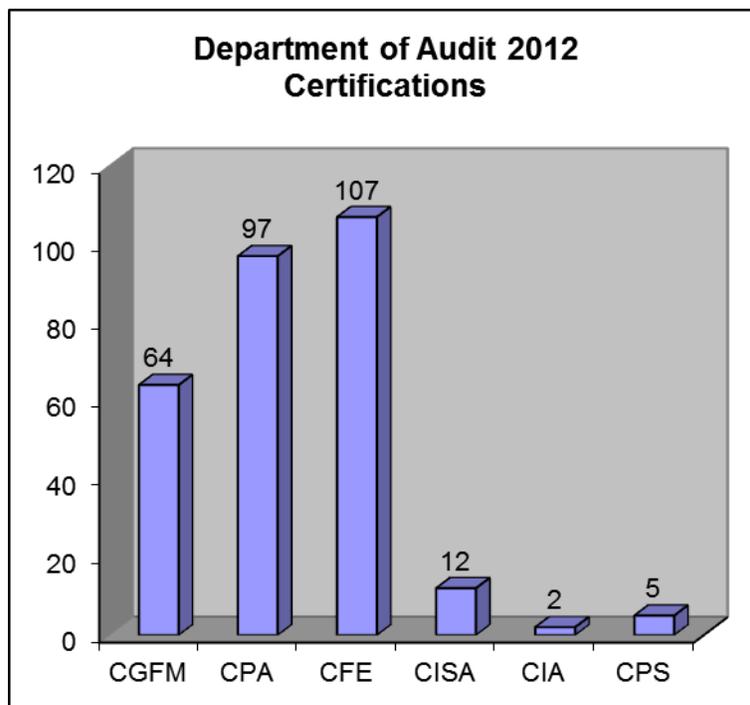
The department's professional staff perform a wide variety of audit work requiring different types of training and experience. Therefore, members of the staff have degrees in fields such as accounting, public administration, information systems, law, political science, criminal justice, education, and nursing. More than 60 of the professional staff have advanced degrees. The department encourages its employees to pursue professional certifications such as Certified Public Accountant, Certified Information Systems Auditor, Certified Fraud Examiner, and Certified Government Financial Manager.

As of June 30, 2012, more than 200 employees of the department had received one or more professional certifications. This range of experience gives a broad

perspective to the department's audit work.

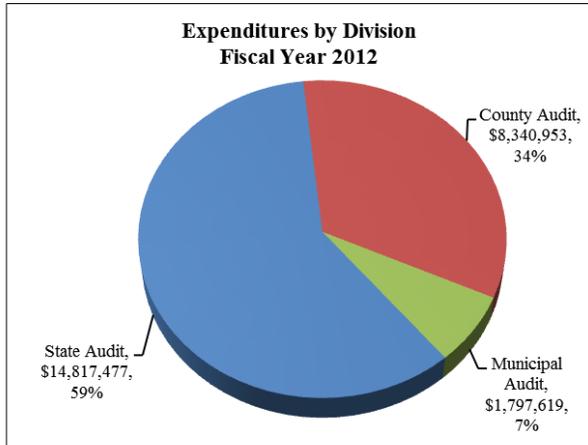
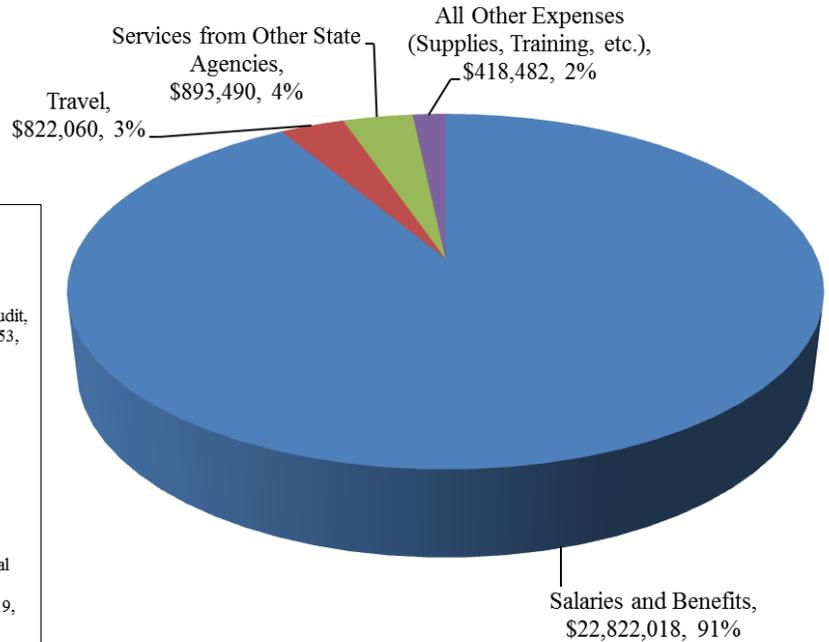
The Department of Audit ensures its auditors receive the required continuing professional education to meet certification standards and Government Auditing Standards. Auditors participate in the department's in-house training program as course developers, presenters, and participants. Over 13,000 hours of training were completed during the fiscal year ended June 30, 2012.

The Department of Audit fully supports its staff's active participation in local and national professional organizations, recognizing that these organizations contribute to the staff's continued growth.



Certified Government Financial Manager (CGFM), Certified Public Accountant (CPA), Certified Fraud Examiner (CFE), Certified Information Systems Auditor (CISA), Certified Internal Auditor (CIA), and Certified Professional Secretary (CPS).

## Department of Audit Expenditures Fiscal Year 2012



### Contact Information

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\* Includes the divisions of County Audit and Municipal Audit.

For additional information on the Department of Audit and the Comptroller, go to  
[www.comptroller.tn.gov](http://www.comptroller.tn.gov).