

Department of Environment and Conservation

May 2005

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STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
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John G. Morgan
Comptroller

May 19, 2005

The Honorable Phil Bredesen, Governor
and
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243
and

The Honorable James H. Fyke, Commissioner
Department of Environment and Conservation
401 Church Street
Nashville, Tennessee 37243

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Department of Environment and Conservation for the period July 1, 2001, through April 30, 2004.

The review of internal control and compliance with laws, regulations, and provisions of contracts or grant agreements resulted in certain findings which are detailed in the Objectives, Methodologies, and Conclusions section of this report.

Sincerely,

John G. Morgan
Comptroller of the Treasury

JGM/th
04/063



STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
DEPARTMENT OF AUDIT
DIVISION OF STATE AUDIT

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May 27, 2004

The Honorable John G. Morgan
Comptroller of the Treasury
State Capitol
Nashville, Tennessee 37243

Dear Mr. Morgan:

We have conducted a financial and compliance audit of selected programs and activities of the Department of Environment and Conservation for the period July 1, 2001, through April 30, 2004.

We conducted our audit in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. These standards require that we obtain an understanding of internal control significant to the audit objectives and that we design the audit to provide reasonable assurance of the Department of Environment and Conservation's compliance with laws, regulations, and provisions of contracts or grant agreements significant to the audit objectives. Management of the Department of Environment and Conservation is responsible for establishing and maintaining effective internal control and for complying with applicable laws, regulations, and provisions of contracts and grant agreements.

Our audit disclosed certain findings which are detailed in the Objectives, Methodologies, and Conclusions section of this report. The department's administration has responded to the audit findings; we have included the responses following each finding. We will follow up the audit to examine the application of the procedures instituted because of the audit findings.

We have reported other less significant matters involving the department's internal control and/or instances of noncompliance to the Department of Environment and Conservation's management in a separate letter.

Sincerely,

Arthur A. Hayes, Jr., CPA,
Director

AAH/th

State of Tennessee

Audit Highlights

Comptroller of the Treasury

Division of State Audit

Financial and Compliance Audit
Department of Environment and Conservation
May 2005

AUDIT SCOPE

We have audited the Department of Environment and Conservation for the period July 1, 2001, through April 30, 2004. Our audit scope included a review of internal control and compliance with laws, regulations, and provisions of contracts or grant agreements in the areas of access to statewide computer applications, information systems, state parks, equipment, the Division of Underground Storage Tanks, citizen support organizations, Tennessee Elk River Resources Management, environmental section receipts, expenditures, Department of Finance and Administration Policy 16 – *Employee Housing and Meals*, and the Financial Integrity Act. The audit was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include approving accounting policies of the state as prepared by the state’s Department of Finance and Administration; approving certain state contracts; and participating in the negotiation and procurement of services for the state.

AUDIT FINDINGS

Access to the State’s Computer Applications Not Adequately Limited*

The department does not adequately limit access to the Property of the State of Tennessee (POST) system, which is used to account for the state’s equipment other than vehicles; the Tennessee On-Line Purchasing System (TOPS), which is used to process purchase orders; and the State Employee

Information System (SEIS), which is used to process personnel actions (page 5).

Inadequate Controls Over the Hospitality Management System and Point of Sale System

There are no written policies and procedures or security violation reports for revenue systems, and there are inadequate controls over gaining access to the systems (page 8).

Weak Controls Over Cash Receipts at the State Parks**

The department does not have adequate controls over cash-receipting procedures at the following state parks visited: Montgomery Bell, Natchez Trace, Old Stone Fort, and Tims Ford (page 13).

Free and Reduced Meal Policy Not Followed at Montgomery Bell State Park*

Montgomery Bell State Park was not following the departmental policy for free and reduced meals for employees (page 15).

Requirements in the Agreements for Leased Operations Not Enforced*

Natchez Trace and Tims Ford state parks did not enforce all requirements of the lease agreements for their leased operations. In addition, proper documentation was not always maintained to determine if correct amounts were paid timely, and the agreements were not always approved before the beginning of the lease term (page 18).

Controls Over Inventories at State Parks Need Improvement*

The department does not have adequate controls over inventory at the following state parks: Montgomery Bell, Natchez Trace, and Old Stone Fort (page 19).

Proper Purchasing Procedures Not Followed**

At Montgomery Bell, Natchez Trace, Old Stone Fort, and Tims Ford state parks, some purchases were not made in accordance with the state's guidelines and/or the department's purchasing procedures. Purchases were not always properly approved. For other purchases, the park should have obtained bids (page 21).

Controls Over Equipment Need Improvement**

The department did not always remove lost or stolen items from POST or report them to the Comptroller of the Treasury timely. For some equipment items tested, the serial number shown in POST was not correct (page 23).

Financial Responsibility Rules Not Enforced**

The Division of Underground Storage Tanks does not enforce its rules requiring tank owners to demonstrate financial responsibility for cleanup costs associated with petroleum leaks (page 27).

Controls Over Underground Storage Tank Expenditures Need Improvement**

The division does not have adequate controls over expenditures for cleanup costs associated with petroleum leaks (page 29).

Underground Storage Tank Fund Is Insolvent

The division has more outstanding requests for reimbursement from tank owners/operators than available funds to disburse, resulting in significant delays in payments (page 34).

Proper Accountability Over Certain Assets Received in 1996 Still Not Established*

Land transferred to the department when the Tennessee Elk River Development Agency was dissolved in 1996 has still not been recorded in the state's inventory system (page 38).

Procedures for Collecting Delinquent Fees Not Followed

The Consolidated Fee Section did not always follow departmental procedures for collecting delinquent fees for the environmental divisions and for calculating penalty and interest on those fees (page 41).

Contracts Not Approved Before Beginning of Contract Period

The department allowed contracted services to be performed before all of the proper approvals of the contracts were obtained (page 44).

Controls Over Community Assistance Grant Expenditures Need Improvement

The department did not have controls in place to detect mathematical errors on invoices or

maintain enough documentation to determine mathematical accuracy. Also, the department did not always pay invoices timely and maintain supporting documentation to support payments. In addition, the department did not require the grantee to comply with all terms of the grant. Lastly, the department did not always obtain all of the required approvals before work began on the grants (page 44).

SPECIAL INVESTIGATION

Lack of Oversight on Propane Purchases Resulted in Lost Cost-Savings

The lack of proper oversight at Fall Creek Falls State Park and Tims Ford State Park resulted in the parks paying considerably more for propane than was necessary (page 52).

* This finding is repeated from the prior audit.

** This finding is repeated from prior audits.

Financial and Compliance Audit

Department of Environment and Conservation

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Financial and Compliance Audit Department of Environment and Conservation

INTRODUCTION

POST-AUDIT AUTHORITY

This is the report on the financial and compliance audit of the Department of Environment and Conservation. The audit was conducted pursuant to Section 4-3-304, *Tennessee Code Annotated*, which requires the Department of Audit to “perform currently a post-audit of all accounts and other financial records of the state government, and of any department, institution, office, or agency thereof in accordance with generally accepted auditing standards and in accordance with such procedures as may be established by the comptroller.”

Section 8-4-109, *Tennessee Code Annotated*, authorizes the Comptroller of the Treasury to audit any books and records of any governmental entity that handles public funds when the Comptroller considers an audit to be necessary or appropriate.

BACKGROUND

The Tennessee Department of Environment and Conservation is responsible for protecting and enhancing the quality of the state’s air, land, and water. It oversees state environmental regulation and management of historic, archaeological, and natural resources and manages Tennessee’s 54 state parks. In addition to the programs that report directly to the commissioner, the department is formally divided into three bureaus: Environment, State Parks and Conservation, and Finance and Business Services.

The Commissioner’s Office oversees all departmental operations. Deputy and assistant commissioners for Environment, State Parks and Conservation, and Finance and Business Services work closely with and report directly to the Commissioner. Also reporting directly to the Commissioner are the department’s general counsel, legislative liaison, and communications office.

Environment is responsible for preserving and enhancing the state’s environmental resources and for ensuring compliance with state and federal regulations.

State Parks and Conservation includes Tennessee State Parks, Recreation Educational Services, and the Tennessee Historical Commission. This bureau manages the system of resort, rustic, and recreational parks and natural, historical, and archaeological areas; provides a systematic approach to constructing, inventorying, and maintaining all facilities managed by the

department; and works to identify and preserve significant historical and archaeological sites, as well as natural resources.

Finance and Business Services provides support and technical assistance for the daily operation of the department, including Fiscal Services, Human Resources, Information Systems, the Policy Office, and Strategic Planning.

An organization chart of the department is on the following page.

AUDIT SCOPE

We have audited the Department of Environment and Conservation for the period July 1, 2001, through April 30, 2004. Our audit scope included a review of internal control and compliance with laws, regulations, and provisions of contracts or grant agreements in the areas of access to statewide computer applications, information systems, state parks, equipment, the Division of Underground Storage Tanks, citizen support organizations, Tennessee Elk River Resources Management, environmental section receipts, expenditures, Department of Finance and Administration Policy 16 – *Employee Housing and Meals*, and the Financial Integrity Act. The audit was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include approving accounting policies of the state as prepared by the state’s Department of Finance and Administration; approving certain state contracts; participating in the negotiation and procurement of services for the state; and providing support staff to various legislative committees and commissions.

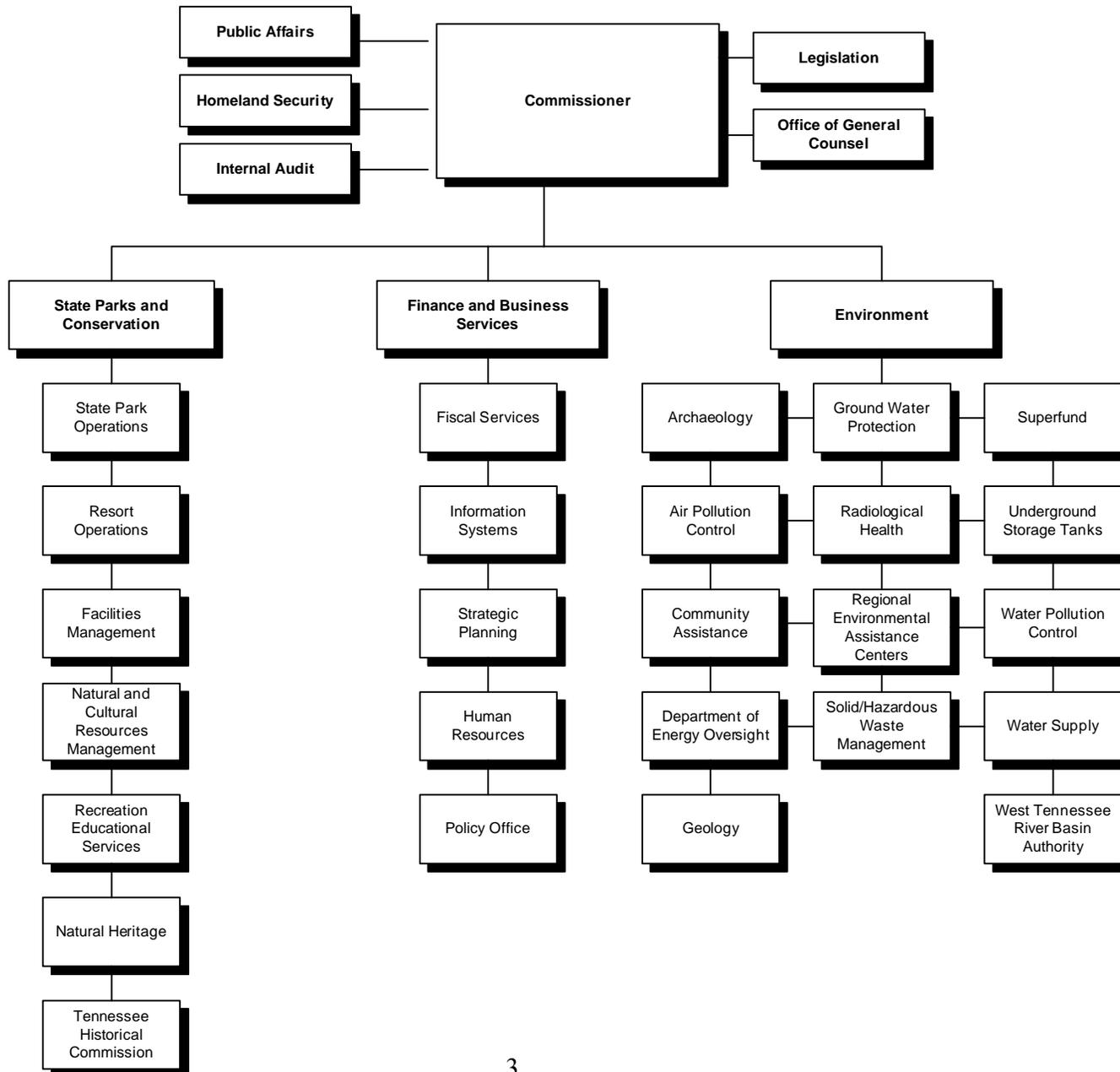
PRIOR AUDIT FINDINGS

Section 8-4-109, *Tennessee Code Annotated*, requires that each state department, agency, or institution report to the Comptroller of the Treasury the action taken to implement the recommendations in the prior audit report. The Department of Environment and Conservation filed its report with the Department of Audit on May 14, 2003. A follow-up of all prior audit findings was conducted as part of the current audit.

RESOLVED AUDIT FINDINGS

The current audit disclosed that the Department of Environment and Conservation has corrected previous audit findings concerning cash receipting for the environmental divisions, environmental assistance centers, and the Fleming Training Center. In addition, the department

Department of Environment and Conservation Organization Chart



has corrected the previous audit finding related to not fully complying with the state policy on providing housing to employees.

REPEATED AUDIT FINDINGS

The prior audit report also contained findings concerning access to the state's computer applications not being adequately limited, weak controls over cash receipts at the state parks, free meal policies not being followed at the state parks, requirements in the agreements for leased operations not being enforced, controls over inventories at the state parks needing improvement, proper purchasing procedures not being followed, weak controls over equipment, financial responsibility rules not being enforced, weak controls over underground storage tank fund expenditures, proper accountability over certain assets not being established, and collection procedures for environmental divisions needing improvement. These findings have not been resolved and are repeated in the applicable sections of this report.

OBJECTIVES, METHODOLOGIES, AND CONCLUSIONS

ACCESS TO STATEWIDE COMPUTER APPLICATIONS

The department uses the Tennessee On-line Purchasing System (TOPS) to handle purchases of goods and services, the State Employee Information System (SEIS) to record payroll and personnel activity, and the Property of the State of Tennessee (POST) system to maintain accountability over its equipment. Our objectives in reviewing this area were to determine whether

- only active employees have access to these applications;
- access is limited to those employees whose job duties require it; and
- the level of access creates an adequate segregation of duties.

To accomplish these objectives, we interviewed key employees to gain an understanding of internal controls. We obtained from the Department of General Services a listing of all persons who had access to Department of Environment and Conservation allotment codes in TOPS as of January 15, 2004, and in POST as of January 7, 2004. We obtained from the Department of Finance and Administration a listing of all persons who had access to Department of Environment and Conservation allotment codes in SEIS as of January 20, 2004. We tested all persons on the listings to determine if they were active employees as of the date of the listings. We tested all persons on the SEIS listing to determine if the level of access was limited to those whose job duties required it. We tested a nonstatistical sample from the TOPS and POST listings to determine if the level of access was limited to those employees whose job duties required it. We tested all persons on the TOPS and SEIS listings to determine if their access

created an inadequate segregation of duties. We tested a nonstatistical sample from the POST listing to determine if the level of access created an adequate segregation of duties.

As a result of these interviews and testwork, we concluded the following:

- inactive employees still had access to some applications;
- access was not always limited to those employees whose job duties required it; and
- the level of access in some instances created an inadequate segregation of duties.

These problems are discussed further in finding 1.

1. The department does not adequately limit access to the state's computer applications

Finding

As noted in the prior audit, the department does not adequately limit access to the Property of the State of Tennessee (POST) system, which is used to account for the state's equipment other than vehicles; the Tennessee On-Line Purchasing System (TOPS), which is used to process purchase orders; and the State Employee Information System (SEIS), which is used to process personnel actions. Management concurred with the prior audit finding and stated that they would reduce user access where necessary and appropriate. Management also stated that they had taken steps to institute procedures for each of the applications to ensure that computer access is canceled promptly after an employee is terminated or transferred. However, issues still remain.

- Testwork was performed on the 17 employees noted in the previous audit with improper access to POST. Of the 17, one (5.9%) still had a greater degree of access than was warranted by his job duties.
- Three of 121 employees tested (2.5%) with access to POST as of January 7, 2004, were not employees of the department as of that date.
- Testwork on 25 employees with access to POST indicated that 2 (8%) had a greater degree of access than was warranted by their job duties. The employees had PROP access, which permits changing all information about a piece of equipment in the department except the cost and surplusing.
- Access at the state parks was reviewed to determine if there were parks with too many individuals with access to POST. It was determined that Edgar Evins State Park, Reelfoot Lake State Park, Pinson Mounds State Park, and Natchez Trace State Park had too many individuals with access.
- Of 200 persons with some level of TOPS access, 26 (13%) had a level of access that created an inappropriate conflict of duties. Sixteen of these were noted in the prior

audit. These individuals could enter a purchase order, approve it, record receipt of the item, and approve payment.

- Testwork on 25 employees with access to TOPS indicated that 4 (16%) had a greater degree of access than was warranted by their job duties.
- Three of 38 employees tested (7.9%) with access to SEIS on January 20, 2004, were not employees of the state as of that date.

Inadequate management controls permit individuals to circumvent the normal review and approval process. This could significantly increase the potential for errors and fraud to occur and go undetected. Failure to end computer access for terminated or transferred employees could allow disgruntled employees or other unauthorized personnel to corrupt files or abuse sensitive information.

Recommendation

The Commissioner should initiate a review of access to all of the state's computer applications. Those employees with more access than is needed should have their access reduced. Employees with access to TOPS should not have the authority to initiate, approve, receive items purchased, and approve payment for purchases. The Commissioner should also establish procedures to ensure that access to computer applications is canceled promptly after an employee is terminated or transferred to another job or department.

Management's Comment

We concur. Appropriate action has already been taken to terminate or reduce the access in most instances noted in the finding. The department is reviewing the computer access of all employees to ensure that the appropriate level of authority is commensurate with the job responsibilities and does not allow one person to perform all aspects of a transaction, whenever possible. There are instances, however, at small state parks where because of the limited staff at those locations, it may out of necessity require one person to have a higher level of access than might normally be warranted. Management will limit these instances to only those that are absolutely necessary.

The department has initiated procedures to ensure that access to computer applications is canceled promptly after an employee leaves their job. The Division of Human Resources will notify the appropriate security administrator when an employee leaves their job. The security administrators for each computer program are then responsible for terminating computer access.

INFORMATION SYSTEMS AT THE RESORT STATE PARKS

The department uses the Hospitality Management System and the Point of Sale system at the resort state parks to account for all cash receipting transactions at the inns, restaurants, gift shops, golf courses, and marinas. These systems were implemented at the resort parks since the last audit. As a result, we decided to perform additional procedures on the Hospitality Management System (HMS) and Point of Sale (POS) information systems to determine whether

- the control environment was adequate;
- policies and procedures manuals and other system documentation were adequate and current;
- high priority program changes were made timely;
- program changes were properly documented and approved;
- access to the system and the utilization of security violation reports were adequate;
- the password policy appropriately hindered access;
- reconciliation procedures were adequate; and
- error correction procedures were adequate.

We obtained an understanding of the control environment through discussions with personnel and through the completion of memos and questionnaires. We reviewed applicable policies and procedures and other system documentation. Also, we obtained and reviewed the program change request log. We obtained a list of users with access to the HMS and POS systems as of April 1, 2004, and selected a nonstatistical sample of these users. To determine if the level of access was proper, we compared the level of access of the users to their job duties. To determine if the department properly canceled access to the systems when employees terminated or transferred employment, we compared the users to a current listing of employees. We asked departmental staff about procedures for security violation reports. We obtained and reviewed documentation of reconciliations performed at the Central Office, and we obtained and reviewed error correction procedures.

Based on our interviews, reviews, and testwork, we concluded that

- high priority program changes were made timely;
- program changes were properly documented and approved;
- the password policy appropriately hindered access;
- reconciliation procedures were adequate; and
- error correction procedures were adequate.

However, we also found that

- the control environment was inadequate;
- policies and procedures manuals and other system documentation were inadequate; and
- access to the system and the utilization of security violation reports were inadequate.

Problems noted above are discussed in finding 2.

2. The department does not have adequate controls over the state parks' Hospitality Management System and Point of Sale system

Finding

The department does not have adequate controls over the state parks' Hospitality Management System (HMS) and Point of Sale (POS) system. The HMS accounts for revenue of the inns and cabins, and the POS system accounts for revenue of retail operations such as gift shops and restaurants. The department began implementing HMS and POS at the parks in 2001. The systems are used by the state's resort parks, which are Paris Landing, Natchez Trace, Pickwick Landing, Henry Horton, Montgomery Bell, and Fall Creek Falls. During the audit, a review of the HMS and the POS system was performed, and many internal control weaknesses were noted.

Based on discussion with various personnel at the department, there are no written policies and procedures regarding the HMS. However, departmental staff did state that they were in the process of developing them. Without policies and procedures, users of the system are not consistent in how they perform the same transactions. Auditors visited two of the resort parks (Natchez Trace and Montgomery Bell) and noticed that reports of the system were being used inconsistently, procedures regarding voids were handled differently, and procedures regarding rates were handled differently.

According to the department's Information Systems manager, currently, there is no security violation report produced to show users who have attempted and/or obtained access to unauthorized areas of the systems. This report could be used by management to detect potential fraud-related activities.

According to staff at Montgomery Bell State Park's gift shop and restaurant, the POS system has the ability to track inventory perpetually. However, the system does not properly subtract items from inventory. Therefore, staff has been unable to utilize this function. In addition, it was observed while at Montgomery Bell that staff had the ability to change the price of an item by using the price override function.

Testwork on cash receipts at Natchez Trace State Park's restaurant and gift shop revealed missing receipts. The close-out reports for one day for both locations were examined to determine if receipts were issued in sequence. This review noted missing receipts. Upon discussion with staff and working with the system, it was discovered that missing receipts occurred when sales transactions were not voided using the void key on the cash register, but instead each item on the receipt was lowered to zero and the cash out button was used. As a result, these transactions or "receipt numbers" would not appear on the close-out report.

Testwork on cash receipts at Montgomery Bell's restaurant, gift shops, and golf course revealed that receipt numbers generated by the POS system are not accounted for.

At Montgomery Bell, it was noted that the POS system's cash drawer was accessed by the employee using a key rather than using the "no-sale" button. This override of the control prevents the system from documenting the number of "no-sale" transactions.

During review of the systems, it was noted that there were no written authorizations for access to the HMS or POS system. Therefore, it could not be determined what level of access was requested, whether the access was appropriately approved, or whether the correct level of access was given based on the request.

Auditors performed testwork on 25 individuals with access to the HMS and 25 individuals with access to the POS system as of April 1, 2004, to determine if their access was appropriate based on their job duties and to ensure that the individuals were still employees of the department as of that date. The results of this testwork were as follows:

- One individual with access to the HMS on April 1, 2004, (4%) was not an employee of the department as of that date.
- Two individuals with access to the POS system on April 1, 2004, (8%) were not employees of the state as of that date.
- Three individuals tested (12%) had a greater degree of access to the HMS than was warranted by their job duties. A building maintenance worker had access to the front desk functions; a laborer had access to the general ledger, management/configuration, night audit, special access, and supervisor functions; and a ranger had access to the housekeeping functions.

Auditors performed an analytical review of a database of POS void reports obtained from central office management of each resort park for various periods from July 2002 to April 2004. It was noted that employees are regularly using user identification numbers in the POS system that do not identify a specific user. This review of void reports revealed that a significant number of voided transactions could not be tied to specific users as follows: Fall Creek Falls State Park – 41%, a total of 2,177 voids; Henry Horton State Park – 68%, a total of 598 voids; Montgomery Bell State Park – 64%, a total of 3,520 voids; Natchez Trace State Park – 25%, a total of 263 voids; Paris Landing State Park – 32%, a total of 863 voids; and Pickwick Landing State Park – 90%, a total of 2,324 voids. Furthermore, it was noted that several individuals that had used their assigned system user name performed an excessive number of voids, and

individuals were noted as having an excessive number of voids classified as “walk-outs.” When park managers and central office management do not require employees to use the correct user identification numbers and monitor this usage, they will not be able to identify a user with a specific transaction. Also, when park managers and central office management are not reviewing and monitoring the void reports, questionable or excessive voids by employees could go undetected.

The department’s internal audit section has issued several reports on the lack of controls over the HMS. As a result of the lack of internal controls, internal audit has performed multiple investigations on employees who have taken advantage of the lack of controls. These reports included investigations on credit card refunds, employees at the park being able to assign managerial access for the HMS to non-managerial employees, and discounted or complimentary rooms being given inappropriately. Other control weaknesses noted by the internal audit section were that one employee, a Hospitality Management Specialist, was responsible for the majority of the HMS business function for all of the resort parks, but there was no backup (an information systems employee’s duties have since been changed to include HMS to help segregate duties and provide a backup). The HMS, by default, does not provide for a detailed audit trail of all transactions in the system. Furthermore, the parks do not have a contingency plan to back up HMS data at an off-site location.

Without proper controls, the potential for errors and fraud to occur and go undetected is significantly increased. Failure to end computer access for terminated or transferred employees could allow disgruntled employees to corrupt files.

Recommendation

The Commissioner should assign specific responsibility for establishing policies and procedures for the HMS. Security violation reports should be created and reviewed by the appropriate management daily to ensure that all access is authorized. Management should make the required changes to the POS system to require the void key on the cash register to be used to void transactions and to account for all receipt numbers. Employees should use the “no-sale” button as necessary rather than opening the cash drawer with a key. Written authorization forms for access should be created and maintained for all employees detailing the level of access requested and documenting all appropriate approvals. Management should continually review and monitor access of all employees to determine if they have the appropriate level of access for their related job duties. Procedures should be established to ensure that access to computer applications is canceled promptly after an employee is terminated or transferred to another job or department. Unique user identification numbers should be assigned to and used by each employee using the HMS or the POS system. The use of generic or temporary accounts should be eliminated and management should monitor this to ensure only authorized user identification numbers are used. Procedures should be developed to obtain written assurances from all HMS and POS users that they understand the correct operating procedures and will obtain management approval for any unusual transactions.

Management's Comment

We concur. The department has formed a Hospitality Management System (HMS) Committee that is in the process of completing a policies and procedures manual. The audit identified areas of concern in the Hospitality Management System that are being addressed by this committee. The audit findings referencing (a) security violation reports, (b) void and no-sale transactions, (c) missing receipts, (d) level of HMS access by employees, (e) unique user identification numbers, and (f) HMS user agreements have been noted and policies and procedures will be created for each area. The department has added an additional employee to help track the progress and implementation of the policies and procedures manual and act as a backup to the Hospitality Management Specialist.

STATE PARKS

We reviewed with parks administration at the central office in Nashville the various controls used to manage the state parks and reports issued by the parks including park policies and procedures. During each audit, we select various parks to visit. We selected the following four parks to visit during this audit: Montgomery Bell, Natchez Trace, Old Stone Fort, and Tims Ford. For those parks, we obtained and reviewed the profit and loss reports prepared by the state parks central office to analyze individual park performance. We obtained listings of park vehicles, gift shop inventories, and golf proshop inventories. We reviewed the most recent internal audit report for each park to be visited to determine if additional audit steps needed to be added. Following this overview, we visited the parks and performed testwork on cash receipts, lease agreements between the parks and vendors, inventories, expenditures, and state vehicle usage.

The objectives of our cash receipts work at the state parks were to determine whether

- cash handling duties at the parks were adequately segregated;
- cash receipts were adequately safeguarded from collection until deposit in the bank;
- cash receipts were deposited timely;
- voids and “no-sale” rings were properly reviewed and approved;
- employees were properly accounting for cash and credit card sales at the golf proshop and other retail operations within the parks;
- gift certificates were handled properly;
- proper rental fees were collected for rooms and/or cabins;
- escrow receipts were properly accounted for; and
- free or reduced meals were only given to eligible employees or others.

At each park visited, we interviewed personnel and performed walkthroughs of procedures to obtain an understanding of internal controls over cash receipts. For each retail operation in the park, we selected a nonstatistical sample of days when there were cash receipts. Old Stone Fort and Tims Ford use manual cash registers, and Montgomery Bell and Natchez Trace use automated systems called the Hospitality Management System (HMS) and Point of Sale (POS) system. At all four parks, we compared cash receipts to the daily sales reports and the deposit slips to determine if the receipts were deposited timely and intact. At Old Stone Fort and Tims Ford, we reviewed cash register tapes for evidence of excessive “no-sale” rings and voids, and at Montgomery Bell and Natchez Trace, we obtained the void reports from each system. We reviewed credit card and gift certificate transactions to determine if they were being properly recorded. For the cabin and inn operations, we compared entries in the escrow receipts ledger to the retail operations report, the sales report for the day, and the deposit slip to determine if proper rates were being charged and all entries in the ledger were being rung up on the cash register or entered into the HMS and deposited timely. As part of our cash receipts testwork at the restaurants, we noted the employees who were given free or reduced meals and determined if the employees had job duties that qualified them.

Based on our interviews, reviews, and testwork, we concluded that

- cash handling duties at the parks were not always adequately segregated;
- cash receipts were not always adequately safeguarded from collection until deposit in the bank;
- cash receipts were not always deposited timely;
- voids and “no-sale” rings were not always properly reviewed and approved;
- employees were not always properly accounting for cash and credit cards sales at the golf proshop and other retail operations within the parks;
- gift certificates were not always handled properly;
- proper rental fees were not always collected for rooms and/or cabins;
- escrow receipts were not always properly accounted for; and
- free and reduced meals were sometimes inappropriately given to employees or others.

These problems are discussed further in findings 3 and 4.

The objectives of our testwork on lease agreements were to determine whether

- the agreements were approved prior to their implementation; and
- the amounts of the payments made by the lessees complied with the terms of the agreements.

We reviewed all leases in effect during the audit period at each of the parks that we visited to determine if the agreements had been approved prior to their implementation. We

tested all payments made by the lessees to determine if the payments complied with the terms of the agreements.

As a result of this testwork, we concluded that the agreements were not always approved prior to their implementation and the amounts of the payments made by the lessees did not always comply with the terms of the agreements. This is discussed further in finding 5.

The objectives of our testwork on inventories were to determine whether proper procedures were followed for safeguarding and accounting for retail inventories. We gained an understanding of the parks' procedures over inventories. We compared the year-end physical inventory count sheets to the inventory totals included on the revenue and expenditure reports sent to the parks administrative office in Nashville. We concluded that the safeguards were not always adequate, and inventory totals on the physical inventory count sheets could not always be reconciled to the totals on the reports sent to Nashville. These are discussed further in finding 6.

The objectives of our expenditures testwork were to determine if expenditures charged to maintenance, professional and administrative, and supplies were properly approved, were supported by an invoice or other appropriate documentation, and were in compliance with applicable policies and procedures. To accomplish this objective, we reviewed the state's and departmental purchasing policies and procedures and obtained an understanding of the internal controls being used. We also tested a nonstatistical sample of expenditures.

We concluded that expenditures were not always properly approved and were not always made in accordance with the state's and/or departmental purchasing guidelines. This issue is discussed in finding 7.

The objective of our state vehicle testwork was to determine if usage of state vehicles by park personnel was proper and adequately documented. We interviewed park personnel about the controls and procedures related to state vehicles. We tested all of the vehicles assigned to the park to determine if the mileage logs were complete and if the reported mileage amounts reconciled to the current odometer readings. For the same vehicles, we obtained from the Department of General Services a listing of Fuelman reports and reviewed them for excessive or unusual usage. We obtained explanations for any excessive or unusual usage. We concluded that state vehicle usage by park personnel was proper and adequately documented.

3. Controls over cash receipts at the state parks are weak

Finding

As noted in the prior four audits of other state parks, the department does not have adequate controls over cash-receipting procedures at the state parks. In its response to the prior audit finding, management stated that they had provided training to all park management on proper internal control procedures and stressed the importance of maintaining adequate documentation. Management also stated that written procedures would be established regarding "no-sale" rings, voids, and other cash controls, and an "Internal Controls Self Audit" would be

distributed to assist resort park management in evaluating their internal controls. Despite additional training and evaluation of controls, problems still remain.

Controls were reviewed over cash receipts at Montgomery Bell, Natchez Trace, Tims Ford, and Old Stone Fort state parks. The following weaknesses were noted:

- Cash receipts were not always deposited timely.
- Voids and “no-sale” transactions on the cash registers were not always reviewed and approved by the supervisor.
- There is a lack of segregation of duties between opening the mail, preparing cash receipts, preparing deposits, and posting to the accounting records.
- There is not always an independent employee who reconciles the mail log, cash receipts, and deposits.
- Excessive daily overages/shortages at each cash receipting location (i.e., restaurant, gift shop, inn, swimming pool) are not always reviewed and documented by management.
- Cash and credit card receipts did not always reconcile to the cash register tapes or daily summary reports.
- In some cases, there was no documentation to indicate that more than one person participated in the count of daily receipts.
- Cash receipts are not always adequately safeguarded. In some cases, there are too many people with access to the parks’ safes.
- Some receipts from the Point of Sale system could not be located.
- Each camping receipt originally has three carbon copies: a white, a yellow, and a pink copy. The white copy goes to the camper, the yellow copy goes with the daily receipts documentation, and the pink is maintained in the receipt book. When a receipt is completed by the Park Ranger, the information is written directly on the white copy and is transferred by carbon to the yellow and pink copies. Amounts were noted as being changed on the yellow copy of the camping receipt, which indicates that the receipt was altered after the original copy was given to the customer.
- Gift certificates/coupons were not consistently voided, entered in the cash register, or maintained.
- At the inns, some customers were charged rates that did not agree with the applicable rate schedule. According to management at the parks, these differences are due to the customers using coupons or receiving state employee discounts. However, no documentation could be provided for the rate variances.

Without the implementation of strong internal controls and proper records being maintained, the probability of an error or fraud occurring and not being detected increases.

Recommendation

The assistant commissioner over state parks should retrain the park managers in proper internal control procedures. The park managers at all state parks should implement procedures to strengthen controls over cash receipts and should closely monitor compliance with these procedures. Cash receipts should be deposited timely. “No-sale” rings should be virtually eliminated and be fully explained and investigated when excessive. Also, the supervisor should approve all voided transactions, and the approval should be documented. Cash-receipting duties should be segregated, or compensating controls should be explained and documented. Current policies and procedures for excessive daily overages/shortages at each receipting location should be followed by management. Cash and credit card receipts should be reconciled to the cash register tapes and the deposits by someone independent of the cash-receipting process. Two employees should count each day’s receipts and initial the daily reports. In addition, access to the various safes at the parks should be kept to a minimum. All documentation and receipts for the day should be maintained with the day’s work. If changes are required on the camping receipts, the reasons for the changes should be documented on the white copy. When they are redeemed, gift certificates/coupons should be canceled, entered in the cash register, and placed with the day’s receipts. At the inns, customers should be charged the rates shown on the applicable rate schedule. If there is a valid reason to deviate from the schedule, documentation should be kept in the customer’s record to explain why a different rate was charged.

Management’s Comment

We concur. The department has decentralized the management structure of Tennessee State Parks. The parks are now managed by four Area Managers who report to the Director of State Park Operations. The addition of the Area Managers and the continued efforts of four Hospitality Services field positions create a management team that will ensure better compliance within Tennessee’s 54 state parks. The department also recognizes that training must be offered continually due to employee turnover and as refreshers to long-term staff. Management has concerns regarding the small staffs at some parks, which will not allow strict segregation of duties without additional staff. The parks will create other checks and balances to alleviate the lack of staffing which is not likely to be corrected with the current budget problems facing state parks.

4. The free and reduced meal policy was not followed at Montgomery Bell State Park

Finding

Some employees of the department are eligible to receive free and reduced meals in certain circumstances. The Department of Finance and Administration’s Policy 16, *Employee Housing and Meals*, states in paragraph 15.b. that meals shall be provided without charge to employees “when it is determined by the appointing authority that situations exist that render it either impractical, unsafe, or imprudent for meal breaks to be taken away from the facility

grounds.” The Department of Environment and Conservation has established policies for providing meals to its employees. However, as noted in the prior audit, this policy was not always followed.

Twenty-six days of restaurant receipts were requested from management at Montgomery Bell State Park. Management could not provide any restaurant receipts for eight (30.8%) of the days requested; therefore, the receipts on these days could not be tested. Testwork on the other 18 days revealed the following problems:

- Thirty-two free meals were provided to employees although their job duties did not entitle them to a free meal. The ineligible employees included a laborer, a custodial worker, a maintenance worker, room clerks, and a secretary. Also, three Department of Transportation employees and a central office employee received a discounted meal.

According to section V.B. of the department’s Policy Directive 301, *Employee Meals-Coffee Breaks*, the following food service employees are eligible for free meals: hospitality managers and assistants, park managers who directly supervise restaurant hospitality managers, restaurant cashiers, cooks, food service aides, servers, storekeepers, maintenance and seasonal employees directly assigned to restaurants and snack bars, and central office staff when directly assigned to the restaurant. According to section VI.A. of Policy Directive 301, “a reduced price meal will be available for employees working at parks with restaurants at a cost commensurate with the expense involved in preparing such meals. The price of this meal will be fifty percent (50%) of the current menu price or buffet price, plus tax.”

- A review of the individual meal receipts revealed that employees received items free that were not eligible. Items received by employees included cokes, desserts, and other non-buffet items. Also, in one instance, an employee ate from the breakfast buffet at 9:00 a.m. In another, a free child’s buffet meal was given to an employee.

Section V.E. of Policy Directive 301 states that “meals will be buffet only, unless unavailable, and include coffee or tea. Desserts, other beverages, or substitute items must be paid for at the regular menu price.” Section V.C. of Policy Directive 301 states that “the breakfast meal is not included [as a free meal], and no free meals will be provided prior to 10 a.m.”

- A review of employee timecards revealed that 37 free meals were provided to employees who did not work two hours before and two hours after the free meal. In two instances, an employee received two free meals during one shift. Also, numerous time cards were not provided by management; therefore, there was no evidence that these employees were on duty two hours before and two hours after the free meals.

Section V.C. of Policy Directive 301 states that “food service employees will receive a free meal only if they are on-duty two (2) hours before and two (2) hours after the meal is consumed. . . . Only one (1) free meal will be allowed for every eight (8) hour shift.”

- Section V.G. of Policy Directive 301 states that “the employee must legibly print and sign their name on their guest check issued by the servitor.” For reduced meals, section VI of Policy Directive 301 states that “each employee must present his/her state ID card for proper identification and sign the check issued by the servitor.”

Signatures on the restaurant receipts could not always be used to determine the name of the employee that received the free meal because some of the signatures were not legible. Therefore, it could not be determined whether the employee was an eligible employee or worked two hours before and two hours after the meal. It was also noted that employees are not always signing their own restaurant receipts. Other individuals are signing for the employee that received the free meal. For example, the server may sign the employee’s name and then initial it.

State parks with the HMS are supposed to utilize the Point of Sale (POS) system to create meal receipts and then print out a listing of all free and reduced meals at the end of the shift. Montgomery Bell State Park is properly utilizing this function; however, management was also keeping an “Employee Meal Register.” The Department’s Internal Audit performed testwork on nine days from the period of June through September 2003 to determine if the amount of free and reduced meals per the meal register matched the amount of free and reduced meals per the POS settlement reports. This review revealed that the meal register had \$492 more for meals than the POS settlement reports. This indicates that not all free or reduced meals are being entered into the POS system.

If employees abuse the free meal policies and proper procedures are not followed, the state loses revenue. If proper records of those receiving free meals are not reviewed and maintained, the likelihood increases that more ineligible employees will receive free meals.

Recommendation

The assistant commissioner over state parks should assess why previous training and distribution of policies and procedures were not effective. Then, new training methods should be developed and implemented at each park. The individual parks’ management should continually monitor the restaurant receipts and POS reports. Central office management should monitor the free meals at each park and investigate unusual or excessive transactions. In addition, parks’ management should ensure that all documentation is properly maintained.

Management’s Comment

We concur. We acknowledge the issues concerning the previous training and compliance of park meal policies. State Parks now has an Inn and Restaurant Management Specialist. This employee will ensure the consistent application of Tennessee State Parks Policy Directive 301 regarding employee meals and will monitor compliance statewide. This policy has been revised to clarify employee eligibility, what times meals may occur, and what food items are available to

employees. Management will institute controls to ensure that documentation related to restaurant transactions is properly maintained.

5. Payments were not made in accordance with the requirements in the lease agreements

Finding

As noted in the prior audit of other state parks, the parks do not enforce all requirements of the lease agreements for leased operations. Management concurred with the prior finding and stated, "Park managers have been instructed to strictly enforce all lease agreements." Management further stated that "the Assistant Commissioner of State Parks has assigned the Contract Administrator to periodically review the lease payments to ensure that lease agreement requirements are followed." However, the Contract Administrator did not perform this function. As a result, multiple discrepancies were noted during the visits to Tims Ford State Park and Natchez Trace State Park. All lease payments, a total of 52 payments, were tested for the marina (24), equestrian center (7), and park store (21) and the following discrepancies were noted:

- Forty-four lease payments (85%) were not received on time. The payments received ranged from one to 31 days late. Per the lease agreement, "the fee shall be paid in advance on the first day of each month." The agreement requires a 10% late charge to be added if payment is not made by the 15th day of the month. Eleven of the 44 lease payments were received after the 15th day of the month. Five of these 11 lease payments did not have a late charge applied to the payment. Five of the 11 lease payments included late charges that were calculated incorrectly.
- Six utility payments for the marina at Tims Ford State Park (11.5%) could not be tested for timeliness of payment because the original statement was not maintained. When the park receives a utility statement, the received date is stamped on the face, and a copy is made. The original is given to the lessee, and the copy is maintained at the park. Five of the six utility statements had a received date on the copy that could not be read. One of the six utility statements could not be obtained from management.
- Seven lease payments received were less than the agreed-upon amount per the lease agreement. Six payments were for the equestrian center at Natchez Trace State Park. Per the agreement, a payment of \$165 per month was to be paid for each month of operation. However, the park permitted the equestrian center to pay only \$100 per month. One payment was for the park store at Natchez Trace State Park. The park store was only open for a partial month during September 2003; therefore, a prorated payment was accepted by the park. Per the agreement, the store is required to be open for the entire month of September.
- Six agreements were reviewed that related to the lease payments tested. Three of the six (50%) were not approved before the beginning of the agreement period. The proper approvals for these agreements were obtained from 38 to 41 days after the beginning of the agreement period.

The failure to enforce lease agreement requirements for operations results in reduced revenue to the state.

Recommendation

The assistant commissioner over state parks should determine why the strict instructions to all park managers “to strictly enforce all lease agreements” were not effective. Furthermore, the Commissioner should determine why the Contract Administrator did not review lease payments. New strategies should be developed and implemented to ensure that leases payments are being reviewed and monitored and that park personnel are strictly enforcing the requirements of all lease agreements.

Management’s Comment

We concur. The Area Managers will be implementing an operational review process that will include evaluations of lease agreements at state parks. Additionally, training will be developed to give park managers a better understanding of the requirements of the lease agreements. A review of all lease agreements up for renewal is ongoing to determine the appropriateness and benefits of these agreements to the department.

6. Controls over inventories at state parks still need improvement

Finding

As noted in the prior audit of other state parks, controls over inventories were not adequate. In its response to the prior audit finding, management stated that it would continue to provide training to park employees regarding the proper segregation of duties for purchasing and receiving merchandise. However, problems remain. Controls over inventories were reviewed at Montgomery Bell, Natchez Trace, Old Stone Fort, and Tims Ford state parks. The following weaknesses were noted:

Montgomery Bell State Park (Dickson County)

- The custodian of the gift shop at the park office is able to directly enter inventory information into the Point of Sale (POS) system and make adjustments to the inventory without any review, and also performs the periodic inventory counts.
- The custodian of the restaurant inventory is responsible for the recordkeeping function and is authorized to purchase and receive inventory.
- Documentation that at least two individuals performed the inventory counts could not be obtained for the inventory at the park office and restaurant. In several instances, the staff indicated that the inventory was counted by only one person.

- The inventory count sheets for the golf proshop, snack bar, and gift shop at the inn for the year end June 30, 2003, could not be provided by park personnel; therefore, the accuracy of the total inventory count sent to the Nashville office could not be determined.

Natchez Trace State Park (Henderson County)

- The restaurant manager is also responsible for the recordkeeping and purchasing functions.
- Gift shop inventories are not adequately safeguarded from theft. The gift shop is directly inside the front door of the Pin Oak Lodge across from the check-in desk. It was observed that personnel are frequently away from the check-in desk and unaware when guests are in the lobby. The employees are not able to see the front door, the front desk, or the gift shop from any of inn's offices.
- Proper documentation is not maintained to ensure that all gift shop items received are entered accurately into the POS system.
- The restaurant inventory count sheet for the year ended June 30, 2003, had a retail total of \$4,206.24. However, the total sent to the Nashville office was \$4,218.16. The difference of \$11.92 could not be reconciled or explained. Also, the gift shop inventory count sheet for June 30, 2003, had a retail total of \$10,156.13. However, the total sent to the Nashville office was \$10,298.60. The difference of \$142.47 could not be reconciled or explained.

Old Stone Fort State Park (Coffee County)

- A park ranger is the custodian of the vending inventory and is also responsible for the recordkeeping and purchasing functions.
- The golf proshop manager is the custodian of the proshop inventory and is also responsible for the recordkeeping and purchasing functions.
- A clerk is the custodian of the gift shop inventory and is also responsible for the recordkeeping and purchasing functions.

If inventory duties are not properly segregated and inventory count sheets are not maintained, the opportunity for fraud is increased. Individuals could order goods and divert them for personal use or could, through collusion with a vendor, order goods which are not delivered but for which payment is made. Fictitious vendors could also be created.

Recommendation

The assistant commissioner over state parks should determine why previous training to park employees on proper segregation of duties of purchasing, recordkeeping, and receiving has not been effective. The assistant commissioner should develop and implement new methods of

training personnel on appropriate inventory procedures. The fiscal year end inventory counts should be properly documented, maintained, and properly approved. Inventory should be adequately safeguarded from theft. The park manager should be the only one authorized to approve adjustments to inventory balances.

Management's Comment

We concur. The areas of concern identified have been addressed with park management. The four new Area Managers are going to help monitor the inventory process and reinforce the policies and procedures governing inventories. Management will seek ways to further segregate the duties of purchasing, recordkeeping, and receiving inventory. The Gift Shop Administrator and the Inn and Restaurant Management Specialist will spot check inventories, review all inventory adjustments, and evaluate segregation of duties. The Hospitality Manager or the Park Manager in charge of the facility will approve inventory adjustments. Maintenance funds will be requested to safeguard inventoried items by enclosing them in a gift shop room or behind glass panels.

7. The state parks still did not follow proper purchasing policies and procedures

Finding

As noted in the prior two audits of other state parks, the state parks did not always follow proper purchasing policies and procedures. In its response to the prior finding, management stated that the Board of Standards had granted state park retail operations an exception to the state's purchasing policy. This exception raised the purchase limit for local purchasing authority to \$1,000 effective December 2001. As a result, during the period under audit, the Department of Environment and Conservation established policies and procedures for purchasing at the state parks. Policy number 2 says that all purchases will be approved according to established spending limits, and purchases up to \$1,000 should be approved by the appropriate program manager (inn, marina, golf course, restaurant, maintenance, gift shop, or administrative). In addition, Policy number 1 prohibits invoice splitting and states the definition of invoice splitting, "Repetitive buying within a calendar month to keep purchases under a specific dollar limit to avoid approval of a greater purchase value." However, split invoices were noted during testwork.

Testwork on expenditures at the four state parks visited revealed that some purchases were not made in accordance with the park's purchasing guidelines. Competitive bids were not obtained for some of the purchases because they were split into multiple invoices. Some of the purchases were not appropriately approved and were paid twice. The problems noted at each park are as follows:

- Seven of 25 purchases tested at Old Stone Fort State Park (28%) were not approved by the appropriate person; one of the seven was not paid timely.

- Eight of 25 purchases tested at Tims Ford State Park (32%) were not approved by the appropriate person.
- Fifteen of 25 purchases tested at Natchez Trace State Park (60%) were not approved by the appropriate person.
- Six of 25 purchases tested at Montgomery Bell State Park (24%) were not approved by the appropriate person. Two of 25 purchases tested (8%) were split into multiple invoices to avoid greater approval and proper bidding procedures. In addition, 2 of 25 invoices tested (8%) were paid twice totaling \$656.62 in overpayments.

As a result of the split invoices noted above and the inadequate segregation of duties noted in the Tennessee Online Purchasing System (TOPS) access testwork in finding 1, it was decided that auditors would search for potential fraudulent transactions at 13 state parks where these purchases were made. At these 13 state parks, a listing was obtained of all non-contract TOPS purchases charged to printing, utilities, communications, maintenance, supplies, vehicles, unclassified, and equipment during fiscal year 2003. The listing contained no purchases greater than \$400; this dollar amount is the threshold for requiring additional approval in TOPS. Some of these invoices were obtained from management and revealed no indications of inappropriate purchases; however, multiple instances of split invoices were noted.

Failure to follow state purchasing policies could result in the park paying too much for a particular product or service or could result in purchases that upper management would have deemed unnecessary or inappropriate. The splitting of invoices is a clear circumvention of purchasing policies and should not be tolerated by management.

Recommendation

The assistant commissioner should determine the reason why state park personnel continue to disregard the importance of following state purchasing policies. The department should monitor compliance with these policies, and take disciplinary action against those park employees who do not fully comply. Top management should establish an effective control environment, which is the foundation for all other components of internal control: risk assessment, control activities, information and communication, and monitoring.

Management's Comment

We concur. A new management team has been created consisting of four Area Managers, four Area Clerks, and four Hospitality Specialists that will be implementing an operational review process to ensure compliance with purchasing policies and procedures. We will continue to train employees responsible for purchasing at parks to ensure that proper procedures are followed, split invoices are eliminated, and bids are obtained when required. Additionally, state parks are now utilizing a payment card system that requires a more thorough

review of all purchases less than \$400. The submission of all purchases made by payment card for review should reduce split invoices and inappropriate expenditures.

EQUIPMENT

The objectives of our work related to equipment were to determine whether

- proper physical security was maintained over the department's equipment;
- the information in the Property of the State of Tennessee (POST) system about equipment assigned to the department was correct; and
- proper procedures were followed concerning lost or stolen equipment.

We interviewed personnel and reviewed procedures to gain an understanding of the procedures for physical security and for adding, deleting, and updating equipment information in POST. We selected a nonstatistical sample of equipment in POST at January 7, 2004, costing at least \$5,000. These items were tested to determine whether the item could be physically located, the description in POST matched the item, and the item had a state property tag. We obtained a list of all equipment reported to our office as lost or stolen as of July 28, 2003. From this list, we selected a nonstatistical sample to determine whether the items were removed from POST timely and were reported to our office timely.

As a result of our review and testwork, we concluded that

- physical security over equipment was adequately maintained;
- the information in POST about equipment assigned to the department was not always correct; and
- proper procedures were not always followed for lost or stolen equipment.

The problems mentioned above are discussed further in finding 8.

8. Controls over equipment still need improvement

Finding

As noted in the prior two audits, the department needs to strengthen controls over equipment. Management concurred with the prior finding and stated that it would continue working on steps to improve the controls over equipment. Management also stated that it had issued written procedures over state-owned property and would monitor to ensure that staff follows the established written procedures; however, further improvement is needed.

A sample of 25 equipment items reported lost or stolen was selected to determine if the equipment was removed from the Property of the State of Tennessee (POST) system and reported to the Comptroller of the Treasury within 30 days of the date that the equipment was reported missing. Of the 25 items tested, 21 (84%) were not removed from POST within 30 days, and 6 (24%) were not reported to the Comptroller's office within 30 days.

Section 8-19-501, *Tennessee Code Annotated*, states, "It is the duty of any official of any agency of the state having knowledge of shortages of moneys of the state, or unauthorized removal of state property, occasioned either by malfeasance or misfeasance in office of any state employee, to report the same immediately to the comptroller of the treasury."

The department has a total of 445 pieces of equipment that cost at least \$5,000, which is the capitalization threshold (the level at which an item is added to inventory). For 11 of these items (2.5%), there was no indication in POST that they had been physically inventoried at the end of fiscal year 2003. The *POST User Manual* requires each state agency to take an annual physical inventory of all property on POST prior to the close of each fiscal year.

Testwork was performed on a sample of 25 equipment items that were listed as active in POST and cost at least \$5,000. Five of the 25 items tested (20.0%) had serial numbers that did not agree with the number shown in POST.

Failure to properly record and inventory equipment weakens accountability and may result in the loss of equipment.

Recommendation

The fiscal director should ensure that the property officer removes lost or stolen items from POST and reports them to the Comptroller of the Treasury immediately, that a physical inventory of all equipment is performed annually, and that information is correctly recorded in POST. The fiscal director should monitor controls over equipment to ensure that all applicable regulations and procedures are followed.

Management's Comment

We concur. The Division of Internal Audit (DIA) has instituted procedures to promptly notify the Comptroller's Office when equipment is reported lost or stolen. If the DIA determines that further review is warranted to conclude whether the items were actually lost or stolen, this process might take longer than 30 days. However, the DIA will document the circumstances in these instances.

On August 19, 2004, the Department reported numerous equipment items to the Comptroller's Office that were believed to have been sent to Surplus Property without maintaining documentation. This initiated the process to remove these items from our

equipment inventory. Most of these were old items that had not been inventoried for several years. This action should bring the department's equipment inventory up to date.

The equipment items found as having incorrect serial numbers have been corrected on POST. The Division of Fiscal Services is sending a memo to all division property officers to confirm serial numbers during the annual equipment inventory.

DIVISION OF UNDERGROUND STORAGE TANKS

The primary functions of this division are to inspect new tank installations and to investigate and oversee the cleanup of leaking petroleum underground storage tanks.

The division's rules and regulations require owners or operators of petroleum underground storage tanks to demonstrate that they are financially able to correct accidental releases and to compensate third parties for bodily injury and property damage caused by the releases.

An owner or operator can demonstrate financial responsibility by participating in the department's Underground Storage Tank Fund, by meeting a financial test of self-insurance, or by using one of the other forms of financial assurance allowed by the U.S. Environmental Protection Agency, provided the owner or operator obtains the approval of the divisions for the alternate form of financial responsibility.

Underground Storage Tank Fund

The purpose of this fund is to provide tank owners or operators with a method of reducing the risk of personal liability for environmental cleanup costs associated with leaks from or the removal of underground storage tanks. All tank owners or operators are now required to participate in the fund, although participation was not mandatory until July 1, 2002. As of this date, all tank owners are required to participate in this fund by paying the annual tank fee and properly registering all tanks.

Fund revenues come from a \$.004 per gallon tax on all gas imported into the state and from annual tank fees paid by the tank owners or operators. Fund expenditures are payments to participating tank owners or contractors for the site cleanups.

The objectives of our review were to determine whether

- management had procedures in place which ensured that tank owners or operators demonstrated financial responsibility;
- management had procedures in place which ensured that cleanup work was only performed by qualified Corrective Action Contractors (CACs);

- management had procedures in place which ensured that all cleanup work done by CACs was satisfactory and that the amount billed for this work was accurate;
- expenditures were approved, properly documented, recorded correctly, and complied with applicable regulations;
- cleanup expenditures were processed for payment timely;
- contracts for cleanup contained the required information;
- management is complying with all laws and regulations related to fund liabilities;
- the fund has a large liability; and
- the fund is behind in paying invoices.

To accomplish our objective, we obtained an organization chart of the division and reviewed the applicable laws and regulations. We interviewed key personnel in the division and reviewed supporting documentation to gain an understanding of the division's procedures. We also tested a nonstatistical sample of UST expenditures from the CACs for cleanup expenditures from July 1, 2001, to November 30, 2004.

As a result of our review and testwork, we concluded that

- management did not have adequate procedures in place to ensure that tank owners or operators demonstrated financial responsibility as discussed in finding 9;
- management did not have procedures in place to ensure that cleanup work was only performed by qualified CACs as discussed in finding 10;
- management did not have procedures in place to ensure that cleanup work done by CACs was satisfactory and that the amount billed for this work was accurate as discussed in finding 10;
- expenditures were approved, properly documented, and reported correctly, but did not always comply with applicable regulations as discussed in finding 10;
- cleanup expenditures were not processed for payment timely as discussed in finding 10;
- contracts for cleanup did not always contain the required information as discussed in finding 10; and
- management is not complying with all laws and regulations related to fund liabilities, the fund did have a large liability, and the fund is behind in paying invoices as discussed in finding 11.

9. The Division of Underground Storage Tanks still does not enforce the rules regarding financial responsibility

Finding

As noted in the prior three audits, the Division of Underground Storage Tanks (UST) does not ensure that owners or operators of petroleum underground storage tanks demonstrate financial responsibility. Chapter 1200-1-15-.08(4)(a) and (b) of the *Rules of the Department of Environment and Conservation* states:

Owners or operators of petroleum underground storage tanks shall demonstrate financial responsibility for taking corrective action and for compensating third parties for bodily injury and property damage caused by accidental releases arising from the operation of petroleum underground storage tanks.

The division's enforcement and compliance section performs on-site inspections to determine whether the owners or operators are complying with the department's rules concerning areas such as installation and leak detection. These inspections include the review of various documents to ensure compliance but do not include verification of the owner's or operator's compliance with the financial responsibility requirements, even though such documents are required to be kept on site. Chapter 1200-1-15-.08(9)(a) states:

Owners or operators shall maintain evidence of all financial assurance mechanisms used to demonstrate financial responsibility under this rule for an underground storage tank. . . . An owner or operator shall maintain such evidence at the underground storage tank site or the owner's or operator's place of business. Records maintained off-site shall be made available upon request of the Department.

Based on discussions with division staff, it appears that the department does not know which owners or operators have fund coverage in the UST Fund until an accidental release occurs. Therefore, it is not possible for the department to determine whether the owner or operator has adequately demonstrated financial responsibility.

In its response to the prior three audit findings, management concurred and stated that it was developing new procedures to address all of the recommendations of the audit. However, these procedures have not been completed.

In June 2001, the department created a financial responsibility section to help various divisions within the department comply with federal regulations regarding financial responsibility. Based on discussions with UST management, there are two positions within this section that are paid for by the UST fund. These positions were created to perform the following two functions:

- To ensure facilities that are not fund eligible submit financial responsibility documentation. This documentation is necessary to prove that the owner/operator can remediate a site, without the help of the fund, if a release should occur.
- To ensure that all facilities submit financial responsibility documentation for the applicable entry level (deductible) to the fund. This documentation is necessary to prove that the owner/operator can pay the applicable entry level to the fund.

However, management disclosed that this section is not performing these functions to ensure that all tank owners/operators comply with the regulations. These employees review financial responsibility documentation if an owner/operator voluntarily submits the documentation; otherwise, they perform financial responsibility duties for other divisions. When brought to the attention of upper management, they indicated that this was a result of a decision of the prior administration. However, no changes have been made since the new administration came into office in January 2003.

Recommendation

The director of the division should promptly establish procedures that require staff to identify the owners or operators who are eligible for fund coverage in the UST fund and review the applicable evidence of financial responsibility for entry level to the fund. The director should then monitor compliance with these procedures. The Commissioner should direct the financial responsibility staff to fulfill their job duties by requiring all tank owners to submit documentation of financial responsibility as required or eliminate the positions to save UST funds.

Management's Comment

We concur. The Department of Environment and Conservation, at the recommendation of the Tennessee Petroleum Underground Storage Tank Advisory Committee (Task Force), will be recommending changes to the UST Act that would change the amount of financial responsibility as well as the fee payment years that must be evaluated to determine fund eligibility. (This Task Force was created by Chapter 925, Public Acts, 2004. This legislation required the Task Force to advise the Commissioner of the Department of Environment and Conservation concerning the petroleum underground storage tank fund, with recommendations concerning revenues and expenditures due December 1, 2004.) The UST Division plans to enforce the financial responsibility requirements once these statutory changes, as well as any regulatory changes necessary to implement those statutory changes, have been made.

10. Controls over Underground Storage Tank Fund expenditures need improvement

Finding

The Division of Underground Storage Tanks (UST) was created in 1988 to protect human health and the environment by preventing future accidental leaks or releases from petroleum underground storage tanks and cleaning up existing petroleum underground storage tank contamination. As of February 2004, there were approximately 5,700 facilities in the state. These facilities are home to approximately 15,600 active underground storage tanks. There were 163 accidental releases discovered during fiscal year 2003 and 172 during 2004.

When an accidental release has occurred, the tank owner/operator can choose a corrective action contractor (CAC) from the division's approved CAC listing to clean up the site. After the tank owner/operator obtains a contract with a CAC and the CAC performs allowable services, the division begins to reimburse the tank owner for costs incurred over the deductible. Testwork was performed to determine whether UST expenditures were appropriate. Problems were noted in the following areas: invoices were not reconciled to the reimbursement requests; contracts were not properly drawn up and approved; requests were not paid timely; CACs were not properly approved; site inspections were not being performed; ineligible services were being reimbursed; and eligible services were being reimbursed at incorrect rates.

The auditor tested a sample of 25 reimbursement requests. Based on testwork performed, the following weaknesses were noted:

- a. Two payments tested (8%) could not be reconciled to the invoices submitted. Based on discussions with UST staff, invoices are not reconciled to reimbursement requests that are \$10,000 or less. Management stated that this policy was implemented because there is not enough staff to review in detail all requests for payments. As a result, the division overpaid these two requests a total of \$124.98.
- b. For the 25 payments tested, there were 22 related contracts. Two of the 22 contracts (9.1%) could not be produced by the UST staff; therefore, only 20 were reviewed. Three of the 20 contracts reviewed (15%) could not be used to determine if the related expenditures were allowable under the terms of the contracts. These three contracts were master contracts, which cover cleanup services for multiple sites of one owner. These contracts require work orders, service orders, or requests for service to be completed that outline the work that is to be performed at each site. Discussions with UST staff revealed that copies of the work orders, service orders, or requests for service are not obtained from the contractor or owner and, therefore, not reviewed as support for payment due to the UST internal policy described in the previous paragraph.
- c. Five contracts tested (25%) were not properly written or approved. Problems noted included not having an express agreement stating whether or not the CAC would use the department's reasonable rate schedule as required by the department's rules. In

one instance, work was performed before the contract was approved, and in another, the contract was not dated.

Section 68-215-129(a), *Tennessee Code Annotated*, states, “(1) All contracts for such services shall be in writing and shall be signed by the owner, operator, or other party obligated to pay for such services. (2) All such contracts shall clearly indicate which charges and costs are required by the department to remediate the petroleum site to acceptable state standards and which charges are associated with work performed for tasks other than the remediation of the petroleum site to acceptable state standards.” Chapter 1200-1-15-.09(16)(b)2(v) of the *Rules of the Department of Environment and Conservation* states that the contract must contain a statement, conspicuously located on the front page of the contract, as to whether the contractor will use the department’s reasonable rate schedule when invoicing for the expenses incurred in the investigation and cleanup of a site.

- d. None of the 25 payments tested were paid timely. The number of days between receipt of the request and the date paid ranged from 70 to 287 days. According to the division’s reimbursement database, the total amount of unpaid claims older than 180 days was over \$11.8 million. This issue has also been noted in the prior three audits. In its response to the prior audit finding, management stated that it was “making a renewed commitment to process all invoices within 45 days after a fully completed application package has been received.” However, this could not be tested because the file did not contain the date that the last item was received to complete the application package.

Three of the 25 payments on reimbursement requests noted above were paid under the Leaking Underground Storage Tank (LUST) fund. This fund is part of a federal program that was created to help with the cleanup costs at abandoned sites and sites where the owner/operator is unwilling to pay. This fund requires a contract between the state and the contractor; therefore, these claims should have been paid within 45 days. Per Section 12-4-703, *Tennessee Code Annotated*,

an agency which acquires property or services pursuant to a contract with a business shall pay for each complete delivered item of property or service in accordance with the provisions of the contract between the business and agency or, if no date or other provision for payment is specified by contract, within forty-five (45) days after receipt of the invoice covering the delivered items or services.

- e. In connection with the 25 payments tested, only 17 different CACs were used for remediation of the sites. However, none of the 17 CACs were properly approved.
 - (1) None of the 17 CACs had filed an up-to-date application with the department. The number of years since the last updated application was received ranged from six to ten years. Chapter 1200-1-15-.09(16)(b)1 of the *Rules of the Department of Environment and Conservation* requires CACs to update their written applications by April 1 of each year.

- (2) None of the 17 CACs had submitted a copy of their contractor's license or copies of their employees' professional licenses and/or registrations as required by Chapter 1200-1-15-.09(16)(b)3(i) and (ii) of the *Rules of the Department of Environment and Conservation*.
 - (3) One of the CACs also did not have an adequate amount of automobile liability insurance listed on the insurance certificate that was submitted to the state.
- f. Eleven facilities (44%) had never had a site inspection performed. Per the *Code of Federal Regulations*, Title 40, Part 281.40(e)(1),

state programs must have inspection procedures to determine, independent of information supplied by regulated persons, compliance with program requirements, and must provide for enforcement of failure to comply with the program requirements. States must maintain a program for systematic inspections of facilities subject to regulations in a manner designed to determine compliance or non-compliance, to verify accuracy of information submitted by owners or operators of regulated USTs, and to verify adequacy of methods used by owners or operators in developing that information.

This issue has also been noted in the prior three audits. In its response to the prior audit finding, management stated that the department was currently developing policies and procedures to ensure that all sites are monitored appropriately and fully documented to the file. It appears that the division has developed a comprehensive inspection plan; however, it has not been fully implemented. It was also noted that due to improper site inspections at the facilities, the division has to rely on the environmental reports that are submitted in support of work that was performed by the CAC. UST management stated that the division's professional geologists and engineers review these reports; however, the reports are not compared to the invoices that are submitted for reimbursement. Therefore, the division does not know if the work invoiced by the CAC is actually performed before reimbursement occurs.

- g. Eight of the 25 payments for the reimbursement requests tested (32%) included services that were considered ineligible or included rates that were not reasonable based on the reimbursement document.
- (1) One of the eight payments reimbursed for a markup by the contractor on a Shelby county permit. Based on a review of the "Reasonable Reimbursement Guidance Document," effective September 1, 2001, markups on utility bills, permits, and leased capital expense items are ineligible costs.
 - (2) Three of the eight payments reimbursed for services at a rate above the maximum allowable rate based on the "Reasonable Reimbursement Guidance Document," effective September 1, 2001. One of the eight payments reimbursed for items

above the agreed-upon rate outlined in the “notice to proceed.” A “notice to proceed” is a document that is required by the contracts for the LUST fund payments that describes the work to be performed and the cost that the division is willing to pay. This document is sent from the division to the contractor.

- (3) Three of the eight payments reimbursed for cleanup that was performed more than one year before receipt of the claim. Chapter 1200-1-15-.09(13)(f) of the *Rules of the Department of Environment and Conservation* states that “an application for payment shall be received within one year from the date of performance or acceptance of the work in order to be eligible for payments from the Fund.”
- h. One facility was initially determined ineligible for fund coverage because the facility did not submit the required release detection documentation. The facility had 30 days to appeal this decision by filing a written petition for a hearing but did not. The facility later submitted the release detection documentation, and the department began reimbursing the facility without following the appeals process required by its rules. Chapter 1200-1-15-.11(1) of the *Rules of the Department of Environment and Conservation* states

Any responsible party . . . who has a right to appeal a determination of the Commissioner by these Rules shall comply with the procedure set forth in this part to perfect an appeal. Such responsible party . . . may petition the Board for a hearing provided a written petition is submitted to and received by the Commissioner within thirty (30) days of receipt of the Division’s determination. The Division’s determination and action shall be final and not subject to review unless the written petition for hearing is submitted and received by the Commissioner within this time frame.

When state laws and division rules and regulations are not followed, UST funds are used to reimburse tank owners/operators for ineligible services. This has contributed to the fund becoming insolvent, which is noted in finding 11. In addition, untimely reimbursing tank owners/operators for eligible fund expenditures could place an undue financial hardship on the tank owners/operators or contractors.

Recommendation

The director of the division should ensure that the contracts between the tank owners/operators and the contractors are properly written and approved. Management should ensure that claims are paid in a timely manner, CACs are properly approved, site inspections are being performed, only eligible services are being reimbursed at the correct rates, and the appeals process is followed. Management should review the instances noted above and determine how they occurred and whether or not they had been identified by staff.

Management's Comment

We concur in part. There are improvements that can be made and some improvements have already been made. However, we do not concur with every detail of the findings, as discussed below.

- a. The division has not used the fast-track approach as a means of processing claims quickly since 2002. At one time the fast-track approach was applied to claims of less than \$10,000. All claims are now given a detailed review and all claimed costs are reconciled.
- b. & c. Contracts are now required to be on file with the division before a tank owner is allowed to receive reimbursement from the fund. The division also reviews the contracts to be sure they contain a statement as to whether the corrective action contractor (CAC) will or will not use the reasonable rate schedule.
- d. At the current time, the division is making an effort to reduce the time between receipt of the request and payment from the UST fund by using temporary employees. This is possible because of additional 2004-2005 revenues that included a one-time allocation of \$10 million for fund reimbursement. Also, legislation (Chapter 925, Public Acts 2004) assessed tank owners a fund maintenance fee that should result in over \$9 million being collected for fund reimbursement. However, once all the money available for reimbursement has been expended, payments will have to be put on hold in accordance with T.C.A. § 68-215-111(f), which states that claims are to be paid subject to the availability of sufficient moneys in the fund.

Payments out of the LUST Trust federal dollars to contractors working for the state are now being paid within 45 days.

- e. Improvements have already been made to the procedure for placing or maintaining corrective action contractors on the division's approved list. The division now requires an updated application annually, as well as copies of licenses and/or registrations. In previous years, the division used the Department of Commerce and Insurance's web site to verify that employees of corrective action contractors were Professional Engineers or Registered Professional Geologists.
- f. The division adopted a policy on June 10, 2002, covering the inspection of remediation equipment installed at a contaminated petroleum site. The division can identify the presence of monitoring wells, but not how the wells were installed, during post-installation site visits. However, to verify all work done at a site for which there is an associated cost would require a division staff member to be on-site several times a year at almost 1,500 sites. Division staff would also have to be present at the offices of contractors to determine if the claims for time spent on clerical work, report preparation, etc. was accurate. This is because much of the site work that is done leaves no visible evidence on site that the work was performed. This is true of sample collection, site surveying, water use surveys, land use determinations, and other tasks performed on-site. The division simply does not have adequate staff to address this

aspect of the audit finding. The division must rely in part upon the credentials of licensed and registered professionals who put their professional credibility and livelihood on the line each time they sign a report submitted to the division.

- g. (1) We concur and during claim review the division will continue to look for and deny claims for markups on utility bills and permits.
- (2) The division makes every effort to pay claims in accordance with the applicable reasonable rate schedule (for state fund eligible claims) or the rates established in the contract (for state-hired contractors paid with federal LUST Trust dollars).
- (3) The attorneys for the division advised that the wording in rule 1200-1-15-.09(13)(f) was not written clearly enough to be enforceable. Therefore, the department supported an amendment to the UST Act to specify wording that is more clearly enforceable. T.C.A. § 68-2125-111(e) was amended, effective July 1, 2004, to state: *“On or after July 1, 2004, all applications for payment of costs of cleanup shall be received by the division within one (1) year of the performance of the task(s) covered by that application in order to be eligible for payment from the fund.”*
- h. We concur. The division will attempt to follow the legally mandated steps in the appeals process in the future.

11. The Tennessee Underground Storage Tank Fund has become insolvent

Finding

The combination of the issues noted in finding 10 and the issues noted below have been major contributing factors to the insolvency of the Underground Storage Tank (UST) Fund. For fiscal years 1999, 2000, and 2003, the fund had a larger amount of claims pending processing than was available in the fund to pay claims. After a review of various fund databases and discussions with UST management, auditors noted numerous areas of concern. Management of the fund has had various corrective actions available over the years that could have been considered to ensure the solvency of the fund; however, they have not been utilized.

Claims Pending Processing

Under Section 68-215-111, *Tennessee Code Annotated*, tank owners who pay the annual registration fee and comply with division rules and regulations may apply to the fund for reimbursement of cleanup costs. Tank owners also apply to the fund for reimbursement for third-party claims, which are any civil actions charging damages to person or property as a result of contamination from leaking tanks. The fund will provide coverage for such claims involving bodily injury and/or property damage caused by leaking tanks. Fund liability is limited to \$1

million per site per occurrence. Owners must pay deductibles, based on the number of tanks owned, before receiving compensation.

As of June 30, 2003, the UST division reported that the UST fund had approximately \$21.2 million in pending claims for reimbursement for actual cleanup costs resulting from leaking tanks. Department management explained that the dollar amount listed for claims pending processing does not take into consideration claims that may be deemed ineligible and claims that may not recover the full amount claimed. According to department personnel, the amount the division actually pays in claims is usually less than the dollar amount listed for claims pending processing due to ineligible claims and deductibles. Based on a review of the reimbursement database, approximately 75 percent of the amounts of claims pending processing are actually paid.

The *Tennessee Comprehensive Annual Financial Report* for fiscal years 1999, 2000, and 2003 have reported a zero fund balance for the UST fund. Fiscal years 2001 and 2002 show a positive fund balance; however, beginning in fiscal year 2001, approximately \$2.3 million was reduced from claims pending processing because it represented funds that were due to state-owned facilities. Accounting principles require that the amount of claims pending processing be included as expenses; however, the total of those claims is computed and presented by UST division staff prior to reviewing the claim for eligibility and allowable reimbursement. The revenues, expenditures, and fund balance for each of the last five years are presented below.

Underground Storage Tank Fund Balances

	Fiscal Year <u>1998 - 1999</u>	Fiscal Year <u>1999 - 2000</u>	Fiscal Year <u>2000 - 2001</u>	Fiscal Year <u>2001 - 2002</u>	Fiscal Year <u>2002 - 2003</u>
Beginning Fund Balance *	\$ -	\$ -	\$ -	\$ 934,000	\$ 72,000
Revenue *	21,336,000	21,710,000	21,973,000	21,226,000	21,253,000
Expenditures *	21,336,000	21,710,000	21,039,000	22,088,000	21,325,000
Ending Fund Balance *	\$ -	\$ -	\$ 934,000	\$ 72,000	\$ -
Claims Pending Processing **	\$ 13,937,000	\$ 17,675,000	\$ 7,650,000	\$ 8,432,000	\$ 21,150,000
Liabilities *	12,855,000	15,612,000	8,478,000	8,402,000	7,668,000
Fund Balance Per UST Division ***	\$ (1,082,000)	\$ (2,063,000)	\$ 1,762,000	\$ 42,000	\$ (13,482,000)

* Source: Amounts obtained from the *Comprehensive Annual Financial Report*, fiscal years 1999 through 2003.

** Source: Dollar amount of claims pending processing as reported by the Division of Underground Storage Tanks.

*** Ending Fund Balance – Claims Pending Processing + Liabilities

Corrective Actions Not Utilized

The following are several corrective actions that UST management has not utilized to reduce liabilities and increase fund balances to be in compliance with Section 68-215-110(e), *Tennessee Code Annotated*, which is noted below.

- Sections 4-3-902 and 4-31-903, *Tennessee Code Annotated*, authorize the Tennessee Local Development Authority to issue bonds up to \$15 million and the proceeds to be used “for the reimbursement of reasonable and safe cleanup of petroleum sites.” However, no bonds have been issued.
- The UST board has not sought legislative approval to increase the amount of deductible that the responsible party must pay before the fund would start incurring costs.
- The UST board has not sought legislative approval to eliminate the contradictory legislation related to increasing the annual tank fee or the petroleum assurance fee. Section 68-215-110(e), *Tennessee Code Annotated*, states that “the board shall, by regulation, adjust underground storage tank fees to a level necessary to maintain a minimum unobligated balance of two million dollars (\$2,000,000).” Based on discussions with management, the board cannot adjust the fee due to Section 68-215-109(a), *Tennessee Code Annotated*, which states that

the board shall promulgate regulations stipulating which petroleum underground storage tanks are subject to fees, the due date of such fees, and the amount of such fees, annually in an amount not to exceed one hundred twenty-five dollars (\$125) per tank. The fee for each petroleum underground storage tank shall be one hundred twenty-five dollars (\$125) per tank starting April 30, 1990.

This part is contradictory to Section 69-215-109(b), *Tennessee Code Annotated*, which states that “the fee may be reviewed and revised as needed by the board based on changes in anticipated fee collections and projected program or fund expenditures.” It is also contradictory to Section 68-215-110(e), *Tennessee Code Annotated*, which was previously noted. The fee has not been revised in 14 years.

As a result of the insolvency of the fund, the state is not in compliance with applicable laws and regulations. In addition, legitimate expenditures incurred by tank owners/operators are not being reimbursed timely as noted in finding 10. The continued practice of paying UST expenditures as funds are available will not correct itself over time.

Recommendation

The Underground Storage Tank Board, in conjunction with the department, should propose a long-term solution that will ensure the solvency of the fund and provide for a regulatory program to ensure ongoing compliance.

Management's Comment

We concur. The claims made against the fund outpaced revenues received by the fund in 1997. The gap between income and expenditures has continued to grow since 1997.

The division investigated the issuance of bonds and learned that the issuance of bonds was not feasible. The costs to the state would exceed the benefit. Also, bonds would only be a temporary solution. Once the time came to pay off the bonds, those debts take priority to all other debts, so that fund reimbursements would be deferred until the bonds were paid off.

The Task Force has advised the department to seek higher deductibles for owners of a small number of tanks. The Task Force has also recommended a higher tank assessment fee based on the number of compartments not just the number of tanks. These are not long term solutions, which the audit findings recommend, but the Task Force wants to wait on the results of some operational changes, such as using a more "risk based" approach to remediating contamination before making recommendations for long-term solutions. The department plans to propose legislation in 2005 that will extend the Task Force's term until June 30, 2007.

CITIZEN SUPPORT ORGANIZATIONS

In 1993, the Tennessee General Assembly passed legislation which officially sanctioned the forming of "citizen support organizations" to "maintain and enhance the purposes, programs and functions of the state park system, including, but not limited to, educational, interpretative and recreational functions."

Two citizen support organizations—Friends of Cedars of Lebanon and Friends of Long Hunter State Park—were reviewed. Our objectives were to review selected internal controls and procedures.

We obtained copies of the organizations' agreements with the Department of Environment and Conservation, lists of the organizations' officers; all bank statements and reconciliations for the period July 1, 2001, through March 31, 2004; minutes of all organization meetings; and supporting documentation for all receipts and disbursements. We reviewed the minutes of all meetings from July 1, 2001, through April 20, 2004. To gain an understanding of procedures and controls over cash receipts, cash disbursements, donations, and compliance with applicable state laws and regulations, we interviewed officers of the organizations. We reviewed the agreements with the department to determine if the terms complied with applicable state laws

and regulations. We obtained bank confirmations as of June 30, 2003, and we reviewed all bank account activity and supporting documentation for receipts and disbursements shown on the bank accounts.

We concluded that the organizations need to improve controls over their financial activities. We believe these two support groups should review the audit report on other citizen support organizations issued by this office dated November 5, 1997, and implement the report's recommendations.

TENNESSEE ELK RIVER RESOURCES MANAGEMENT

The Tennessee Elk River Development Agency (TERDA) was created in 1963 by the Tennessee General Assembly to develop and implement a program of comprehensive resource and economic development for portions of the Elk River watershed. In 1971, the Tennessee Valley Authority deeded the agency certain land surrounding the Tims Ford Reservoir for development.

The Tennessee General Assembly, in Public Chapter No. 816, dissolved the agency as of April 26, 1996. All powers, duties, contractual obligations, and functions of the agency were transferred to the Tennessee Department of Environment and Conservation. In addition, all interests in real property and in water rights held by the agency were transferred to the department. The department accounts for these activities as Elk River Resources Management.

The objective of our review of this area was to determine whether the assets that were transferred from TERDA when it was dissolved have been properly recorded in the state's inventory systems.

To accomplish our objective, we interviewed key personnel and reviewed the state's inventory systems. As a result of this review and testwork, we concluded that all assets, except for land, have been recorded in the state's inventory system. See finding 12.

12. The department has not established proper accountability over certain assets

Finding

When the Tennessee Elk River Development Agency (TERDA), now called Tennessee Elk River Resources Management (TERRM), was dissolved in 1996 by the Tennessee General Assembly, the state transferred the assets of the agency to the Department of Environment and Conservation. The prior audit noted that some of these assets had not been added to the state's inventory systems. In its response to the prior-year finding, management concurred and stated that the department had taken appropriate action to ensure that the recreation facilities, buildings, and water system were properly recorded. In addition, management stated that they would continue to work with the Department of Finance and Administration, Real Property

Management Division, to properly record the land on the state's financial statements. The other assets have been properly recorded; however, the land that TERDA had recorded at \$3,933,740 has not been added to the state's inventory system.

When assets are not properly accounted for, state regulations are violated and the assets are not properly reported in the state's financial statements.

Recommendation

The Commissioner should instruct the appropriate staff to work with the Department of Finance and Administration to record the land in the state's inventory system.

Management's Comment

We concur that not all of the TERDA properties have been included in the state's inventory system. The department has taken the following actions regarding the recording of land: (1) A spreadsheet regarding the TERDA properties has been submitted to the Department of Finance and Administration (F&A). The spreadsheet contains the reservoir project tract number, seller name, acreage, purchase price, and the book and page number of the deed of conveyance for the original land acquisitions; and (2) On November 5, 2004, the department sent electronic maps and property descriptions to F&A. Those maps and descriptions were prepared from recent surveys and cover approximately 2,000 acres of former TERDA land. We will continue to work to satisfy F&A's requirements to record the TERDA properties in the state's inventory system.

ENVIRONMENTAL SECTION RECEIPTS

The Environmental Section has 14 divisions plus 8 Environmental Assistance Centers which are located across the state. Nine of these divisions and all of the Environmental Assistance Centers receive payments for fees, permits, and licenses. The divisions include Superfund, Underground Storage Tanks, Radiological Health, Solid/Hazardous Waste Management, Air Pollution Control, Ground Water Protection, Water Supply, Water Pollution Control, and Community Assistance (which includes the Fleming Training Center). The fees received from the organizations regulated by these divisions provide practically all of the operational funding.

The objectives of our testwork in this section were to determine whether

- cash receipting duties in the Consolidated Fee Section in Nashville, the Environmental Assistance Centers, and the Fleming Training Center were adequately segregated;
- controls over the issuance and usage of receipt books were adequate;

- access to the databases used to update customer payments to the department for fees and permits was adequately controlled;
- receipts were reconciled to deposits and updates to accounting records; and
- the Consolidated Fee Section followed proper procedures for collecting delinquent fees.

To accomplish our objectives, we reviewed all applicable policies and procedures. In the Consolidated Fee Section in Nashville, where most customer payments are received, we completed internal control questionnaires and flowcharts to gain an understanding of office procedures, to determine if cash-receipting duties were properly segregated, and to determine if access to the customer databases was adequately controlled. We observed the office's handling of receipt books to determine if the controls were adequate. We tested a nonstatistical sample of receipts of the nine divisions of the environmental section from July 1, 2001, to March 19, 2004, to determine if the receipt information reconciled to the bank deposit and the updates to the customer databases. We also tested a nonstatistical sample of late payments made to the department from July 1, 2001, to May 19, 2004, to determine if the Consolidated Fee Section was following proper procedures for collecting delinquent fees.

We visited two of the eight Environmental Assistance Centers (Nashville and Jackson). The centers house the offices of the environmental specialists who serve as field inspectors for a particular part of the state. Some centers have employees from as many as eight divisions. Customers can also pay their fees at these centers. The payments that are received at the centers are deposited at local banks near the centers. At the centers visited, we interviewed the staff and completed internal control questionnaires to gain an understanding of the cash-receipting procedures and to determine if duties were properly segregated and receipts were issued and accounted for appropriately. We tested nonstatistical samples of receipts at the Nashville and Jackson centers from July 1, 2001, to February 18, 2004, and March 5, 2004, respectively, to determine if the receipt information reconciled to the bank deposit. The staff at the centers did not have access to the customer databases. The updates to the databases are performed in Nashville by the Consolidated Fee Section.

We also visited the Fleming Training Center. The center provides training classes for water treatment and waste water treatment operators and administers certification examinations. The training classes are free, but there is a charge to take the exams and to maintain the certification. Payments for the exams and certifications are received at the center. We interviewed the fiscal staff of the center to gain an understanding of the cash receipting duties and to determine if they were properly segregated. We tested a nonstatistical sample of receipts from July 1, 2001, to February 10, 2004, to determine if the payments made by the applicants could be reconciled to a bank deposit and if the deposits were made timely. For receipts received after the applicable deadline, we reviewed documents to ensure that late fees were properly assessed.

As a result of all of the above interviews and testwork, we concluded that

- cash-receipting duties at the central office, the Environmental Assistance Centers, and the Fleming Training Center were adequately segregated;
- controls over the issuance and usage of receipt books were adequate;
- access to the databases used to update customer payments to the department for fees and permits was adequately controlled; and
- receipts were adequately reconciled to deposits and updates to accounting records.

However, the Consolidated Fee Section did not always follow proper procedures for collecting delinquent fees (discussed in finding 13).

13. The Consolidated Fee Section did not follow departmental procedures for collecting delinquent fees

Finding

The Consolidated Fee Section did not always follow departmental procedures for collecting delinquent fees for the environmental divisions and for calculating penalty and interest on those fees.

The department's Environmental Protection Fund Late Payment Penalty and Interest policy, Section 5.1, requires the envelope with the postmark date to be retained if a payment is not made timely. However, for 27 delinquent fees tested, the envelope was not retained. If the envelope with the postmark date is not retained, the division will not have proper documentation to support its assessment of penalty and interest on late payments.

When a payment is not received on time, a second invoice is supposed to be sent 20 days after the due date. However, second notices were not sent for two delinquent fees tested, and second notices were not sent timely for 14 delinquent fees tested. The prior four audits have noted that the Division of Water Pollution Control did not exert sufficient effort to collect delinquent accounts. In response to the prior audit finding, management concurred and stated that a schedule had been implemented indicating the dates to mail delinquent notices. However, problems remain. Section 5.6 of the policy requires the second invoice to clearly state, "This amount due must be received no later than the last day of the month to avoid additional penalty and interest." However, two invoices tested did not contain this required statement.

The department's policies and Section 68-212-110(e), *Tennessee Code Annotated*, require penalty and interest to be imposed on any fees not paid by their due date. These guidelines specify how the penalty and interest are to be calculated. However, for eight delinquent fees tested, insufficient penalty and interest were assessed. For four delinquent fees tested, too much penalty and interest were assessed, and no refund or credit was given to the payer. For four delinquent fees tested, no original billing invoice was documented in the payer's file, and the fee coordinator could not provide an explanation of how the penalty and interest were assessed.

When delinquent fees, penalty, and interest are not paid within 30 days of the second notice, the department's policy requires the account to be forwarded to the department's Office of General Counsel (OGC) for collection. However, three delinquent fees tested were not turned over to OGC.

When a payer verbally agrees to pay the fee, penalty, and interest, documentation of the agreed-upon amount and payment due date are required to be filed in the payer's file. However, subsequent contacts with the payers regarding two delinquent fees tested were not documented.

If proper procedures for handling delinquent accounts are not followed, chances of collection greatly decrease, and revenue may be lost.

As noted in the prior audit, the written departmental policies and procedures for delinquent accounts have not been updated since the establishment of the Consolidated Fee Section. Management concurred and stated that they were working with a contractor to edit and update the policies and procedures for all fee section responsibilities and functions, as well as the collection of delinquent accounts, to include each deadline in the collection process. However, this has not been completed.

Recommendation

Management should ensure that employees follow the established written departmental policies and procedures for collecting delinquent fees and for calculating penalty and interest on those fees. Management should monitor and take appropriate actions against those employees who do not follow the policies. The department's policies should be updated to include the Consolidated Fee Section.

Management's Comment

We concur. Management will ensure that procedures are followed. Internal standard operating procedures have been developed for the consolidated fee section. Management of the consolidated fee section will monitor compliance against the established procedures. The department's policies relative to the collection of fees will be updated to reflect the establishment of the consolidated fee section.

EXPENDITURES

The objectives of this section were to determine whether

- expenditures charged to contracts and grants for consulting services and travel by non-state employees were properly supported, charged to the proper allotment code and transaction code, in compliance with applicable regulations and contract or grant terms, and properly approved;

- sole-source contracts of the department were properly approved, reasonable, and in compliance with applicable regulations;
- expenditures for Community Assistance grant expenditures were properly supported, properly approved, and in compliance with applicable regulations; and
- expenditures incurred with state credit cards were reasonable, adequately supported, properly approved, and in compliance with applicable regulations.

We interviewed key personnel and reviewed rules and policies to gain an understanding of the division's procedures and controls over contract management and payment processing. We obtained a list of expenditures charged to contracts and grants for consulting services and travel by non-state employees for the period of July 1, 2001, through November 30, 2003. We selected a nonstatistical sample of expenditures from this list to determine if the amounts paid were proper, allowable, and supported, and that the contracts were appropriately initiated. In addition, we obtained a list of sole-source contracts that the department had entered into during the period July 1, 2001, through January 15, 2004. We reviewed each contract to determine whether the justification for the sole-source contract was proper and if the contract was appropriately initiated. Furthermore, we obtained a list of contracts for Community Assistance for the period July 1, 2001, through November 30, 2003. We selected a nonstatistical sample of expenditures from this list to determine if the amounts paid were proper, allowable, and supported, and if the contracts were appropriately initiated. Lastly, we interviewed key personnel and reviewed policies and procedures to gain an understanding of the state's credit card process. We obtained a list of departmental credit card expenses for the period July 1, 2001, through October 17, 2003. We selected a nonstatistical sample of expenditures from this list to determine if amounts paid were proper, allowable, and supported.

As a result of our review and testwork, we concluded that

- expenditures charged to contracts and grants for consulting services and travel by non-state employees were properly supported, charged to the proper allotment code and transaction code, and in compliance with applicable regulations and contract or grant terms, but the contracts were not always properly approved;
- sole-source contracts of the department were reasonable and in compliance with applicable regulations, but the contracts were not always properly approved;
- expenditures for Community Assistance grants were not always properly supported, properly approved, or in compliance with applicable regulations; and
- expenditures incurred using state credit cards were reasonable, adequately supported, properly approved, and in compliance with applicable regulations.

The problems mentioned above are discussed further in findings 14 and 15.

14. The department failed to approve contracts before the beginning of the contract period

Finding

The department failed to approve contracts before the beginning of the contract period. Of the 53 contracts reviewed, 49 (92%) were not approved by all parties before the beginning of the contract period. The approvals for these contracts were obtained from 7 to 365 days after the beginning of the contract period. However, we did not note any payments made on these contracts before the final contract was approved. Chapter 0620-3-3-.06(3) of the *Rules of the Department of Finance and Administration* states, “upon approval by the Commissioner of Finance and Administration, a contract shall be fully approved.”

If contracts are not properly approved before the contract period begins and before services are rendered, the state could be obligated to pay for unallowable services. The Department of Finance and Administration’s Office of Contracts Review Service Contract Policy .07b states that “the procuring agency head may be held personally responsible and liable should it be necessary to pay for service provided in good faith without a valid, approved contract.”

Recommendation

The Commissioner should ensure that the contract process is initiated far enough in advance to allow the contract to go through the proper channels of approval. Contracts should be approved by all necessary parties before the beginning of the contract period.

Management’s Comment

We concur. Management has taken action to correct this. A Contract Administrator has been hired for the department. The Contract Administrator will help ensure that all contracts are approved prior to the beginning of the contract period. Written policies and procedures will be developed to clearly state management’s expectation of all program staff.

15. Controls over community assistance grant expenditures need improvement

Finding

The Division of Community Assistance provides technical and financial assistance to various communities of the state. A community may be defined as a county, city, utility district, business, industry, school, association, or general public. The division issues approximately 150 grants and 50 rebates, which total approximately \$10 million to help protect the environment. Testwork was performed to determine if expenditures for the Division of Community Assistance were appropriate. Problems were noted in the following areas: invoices were not mathematically correct, invoices were not paid within 45 days, invoices were not in compliance with the contract

terms, contracts were not properly approved before the beginning of the contract term, and work was performed on some of these contracts before the approvals were obtained.

Based on testwork performed, the Division of Community Assistance does not have adequate controls over grant expenditures. The following weaknesses were noted:

- a. Of the 25 invoices tested, 4 (16%) were not mathematically correct, or mathematical accuracy could not be determined. Three of the four invoices noted were not detailed enough to determine the mathematical accuracy of the grant payment. One of the three invoices previously noted contained a “grant balance remaining” column, which was not mathematically correct. One of the four invoices noted contained a “contract expense year-to-date” column, which was not mathematically correct. The incorrect calculation of “grant balance remaining” and “contract expense year-to-date” did not affect the payment amount.
- b. Of the 25 invoices tested, 12 (48%) were not paid within 45 days of receipt of the request. Payments ranged from 48 to 186 days after receipt of the invoice. Per Section 12-4-703, *Tennessee Code Annotated*,

An agency which acquires property or services pursuant to a contract with a business shall pay for each complete delivered item of property or service in accordance with the provisions of the contract between the business and agency or, if no date or other provision for payment is specified by contract, within forty-five (45) days after receipt of the invoice covering the delivered items or services.

- c. Of the 25 invoices tested, 23 (92%) were not in compliance with the terms of the related contract.
 - (1) Twenty-two of the 23 contracts did not have supporting documentation. The division destroys all supporting documentation at the end of each fiscal year. The division’s Records Disposition Authorization requires records of quantity, quality, and waste tires; waste tire shredding reports; and copies of invoices to be retained for five years at the agency and then destroyed.
 - (2) Nine of the 23 contracts state that the “grantee agrees to maintain and submit to the State, on at least a monthly basis, documentation of the tonnage of tires collected each month and of the source of each load of tires collected.” The invoices related to these nine contracts were not submitted to the division at least monthly. The time period between the invoices ranged from one and a half months to eight months. Also, one of the nine invoices was for services that were performed outside the contract term.
 - (3) Seven of the 23 contracts state that “the grantee shall submit invoices, in form and substance acceptable to the State, with all of the necessary supporting documentation . . . Such invoices shall be submitted no more often than monthly.”

The invoices related to these seven contracts were submitted to the division more than once per month.

- (4) One of the 23 contracts states that “the grantee shall be compensated for actual, reasonable, and necessary costs.” The invoice related to this contract was not submitted for actual costs. The grantee divided the contract amount by four and submitted this amount every quarter to ensure the full contract amount was expended. However, after reviewing documentation at the grantee, it appeared that the grantee’s expenses were more than the total amount of the grant received.
- d. None of the 25 contracts tested were approved by all parties before the beginning of the contract period. These 25 contracts are included in the contracts that are discussed in finding 14. Fourteen of the 25 contracts not properly approved also contained evidence that work was performed for the contract before the contract was approved. Chapter 0620-3-3-.07(2) of the *Rules of the Department of Finance and Administration* states that “a signed contract affixed with the signature of all officials required for approval of the contract shall authorize a contractor or grantee to commence work on the subject scope of services.”

The failure to follow proper procedures could result in the state paying for services and goods not received by the state.

Recommendation

The Director of the Division of Community Assistance should develop policies and procedures to ensure that invoices are adequately reviewed before payments are made. The director should assign specific responsibility for monitoring compliance with these procedures.

Management’s Comment

We concur. To ensure that invoices are mathematically correct, a policy/procedural change memo has been given to grants analysts outlining revised monitoring procedures for payments.

Regarding the payment of invoices within 45 days, grants analysts have been instructed to be more diligent in monitoring receipt dates on invoices. Invoices needing additional documentation will be returned if not received in a reasonable time period. The process for awarding grants was improved for fiscal year 2005 which will ensure that grant payments are not being held pending execution of the grant documents. Finally, a policy/procedural change memo has been given to grants analysts outlining better monitoring procedures for payments.

We did not destroy all of the supporting documentation for the contracts. We agree that the majority of supporting documentation for the waste tires contracts for fiscal years 2000-2003

was destroyed. Backup documentation for all other grant programs back to fiscal year 1999 has been retained. Tire manifests were destroyed for fiscal year 2000-2003 because information contained on the tire manifests was recorded in the Division of Community Assistance's (DCA) waste tire database. The Department understands the gross error made in destroying these records. In the future, records will not be destroyed and the Department will comply with the Records Disposition Authorization and audit for the relative grant programs.

Grantees had difficulty in complying with the clause in the contract that required grantees to submit invoices on a monthly basis (due to the varied schedules of pickup and transport to end use by haulers/transporters). This clause has been removed starting with the 2003 grants.

DCA has issued a policy/procedural change memo to staff revising monitoring procedures for payments to ensure that invoices will not be submitted more often than monthly and grantees will not be paid in four equal payments. Staff will monitor grantee invoices to ensure that billings are reimbursed only for actual costs.

An Administrative Services Manager in the Division of Fiscal Services has recently been hired by TDEC to ensure that all contracts will be properly approved before the beginning of the contract period. Furthermore, DCA's process for awarding grants was improved for fiscal year 2005, which will further ensure that grant documents are fully executed prior to the beginning of the contract period.

DEPARTMENT OF FINANCE AND ADMINISTRATION POLICY 16 - *EMPLOYEE HOUSING AND MEALS*

The department has many employees working at parks around the state who need to live at or near the park to be able to respond to emergencies. If possible, the department places the employees in state-owned housing within the park. If this is not possible, the employees are asked to live as close as possible to the park and are paid a housing allowance.

The Department of Finance and Administration (F&A) issued Policy 16 on January 30, 1998, to establish guidelines which ensure compliance with applicable state and federal laws, particularly Internal Revenue Code requirements, governing all housing and meals provided to all officials and employees and to provide a uniform policy addressing all state-owned housing. Because of the number of employees at the department who are subject to the requirements of this policy, we decided to perform testwork on the department's compliance with this policy.

Our objectives were to determine whether

- the department had procedures in place which ensured that F&A Policy 16 was followed;
- employees receiving housing allowances were also living in state-owned housing;
- employees receiving housing allowances satisfied the necessary prerequisites; and
- employees living in state-owned housing had completed all of the required forms.

To accomplish these objectives, we reviewed the policy to gain an understanding of its requirements. We interviewed departmental personnel to gain an understanding of the procedures they used to ensure compliance with the requirements of this policy. We obtained copies of the department's procedures and housing plans issued during the period April 2003 through December 2003. We obtained a listing from the State Employee Information System (SEIS) of all employees who had received a housing allowance during the period July 1, 2001, through December 31, 2003, and compared it to a list obtained from the department of employees who were assigned state-owned housing during this period to determine if any employees were receiving both. We tested a nonstatistical sample of employees who received a housing allowance to determine if their job duties and circumstances permitted it. We reviewed a nonstatistical sample of employees living in state-owned housing to determine if the forms required by Policy 16 were on file.

As a result of our interviews and testwork, we concluded that

- the department did have procedures in place which ensured that F&A Policy 16 was followed;
- employees receiving housing allowances were not shown on the housing plan as living in state-owned housing;
- employees receiving housing allowances satisfied the necessary prerequisites with minor exceptions; and
- employees living in state-owned housing had completed all of the required forms.

FINANCIAL INTEGRITY ACT

Section 9-18-104, *Tennessee Code Annotated*, requires the head of each executive agency to submit a letter acknowledging responsibility for maintaining the internal control system of the agency to the Commissioner of Finance and Administration and the Comptroller of the Treasury by June 30 each year. In addition, the head of each executive agency is required to conduct an evaluation of the agency's internal accounting and administrative control and submit a report by December 31, 1999, and December 31 of every fourth year thereafter.

Our objectives were to determine whether

- the department's June 30, 2003; June 30, 2002; and June 30, 2001, responsibility letters and December 31, 2003, internal accounting and administrative control report were filed in compliance with Section 9-18-104, *Tennessee Code Annotated*;
- documentation to support the department's evaluation of its internal accounting and administrative control was properly maintained;

- procedures used in compiling information for the internal accounting and administrative control report were in accordance with the guidelines prescribed under Section 9-18-103, *Tennessee Code Annotated*; and
- corrective actions are being implemented for weaknesses identified in the report.

We interviewed key employees responsible for compiling information for the internal accounting and administrative control report to gain an understanding of the department's procedures. We also reviewed the June 30, 2003; June 30, 2002; and June 30, 2001, responsibility letters and the December 31, 2003, internal accounting and administrative control report to determine whether they had been properly submitted to the Comptroller of the Treasury and the Department of Finance and Administration.

We determined that the Financial Integrity Act responsibility letters and internal accounting and administrative control report were submitted on time, support for the internal accounting and administrative control report was properly maintained, procedures used were in compliance with *Tennessee Code Annotated*, and corrective actions are being implemented for weaknesses identified in the report.

SPECIAL INVESTIGATION

PROCUREMENT OF PROPANE GAS AT FALL CREEK FALLS AND TIMS FORD STATE PARKS

In December 2002, the Division of State Audit received information that a liquefied petroleum (propane) vendor under statewide contract had possibly overbilled the Tennessee Department of Environment and Conservation for propane deliveries to Fall Creek Falls State Park, located in Van Buren County.

The primary issue presented for this review involved the number of gallons of propane delivered to the park and the appropriate markup. During a week's period, the vendor should have made deliveries in amounts of 5,000 gallons or more rather than multiple small deliveries, each less than 5,000 gallons, because the park had large-capacity tanks (two tanks with the capacity of 20,000 gallons each). Deliveries of 5,000 gallons or more would have cost the department substantially less.

Pursuant to the statewide contract, deliveries of 4,999 gallons or less cost more on a per-gallon basis than deliveries of 5,000 gallons or more. The price per-gallon consisted of a base price plus markup. Base prices vary on a daily basis. The markups in the contract over the base price were \$0.399 for deliveries of 4,999 gallons or less and \$0.109 for deliveries of 5,000 gallons or more. As an illustration, if the daily price per gallon of propane was \$0.50, the price with markups extended to the park would have been \$0.899 per gallon where the delivery amount was less than 5,000 gallons, and \$0.609 where the delivery amount was 5,000 gallons or

more. The difference between the prices of large and small deliveries was \$0.29 a gallon, a significant price reduction for large deliveries.

The state's propane needs were satisfied through statewide contracts between the Department of General Services and various vendors. In this case, park officials utilized the statewide contract and ordered propane from the vendor for that particular area. The propane contracts with the Department of General Services did not specify which party was responsible for ensuring that larger deliveries (5,000 gallons or more) were to be made when possible. The payments under the statewide contract to the vendor for Fall Creek Falls State Park totaled \$320,000 during fiscal years 2000 through 2002.

The objectives of this review were

- to determine whether overpayments on propane deliveries were incurred by Fall Creek Falls State Park;
- to determine the adequacy of internal controls at Fall Creek Falls related to propane purchases; and
- to report the findings to the department and recommend appropriate actions to correct any noted deficiencies.

Scope

During the review, the Division of State Audit interviewed relevant personnel from the Department of Environment and Conservation and the Department of General Services. The multi-year statewide contract (Statewide Contract 215) effective July 1999 and extended through June 2004 was reviewed. Purchase orders, invoices, and related documents for propane purchases at the state parks for the period July 1999 through January 2004 were also reviewed. Vendor invoices were reconciled with the State of Tennessee Accounting and Reporting System (STARS). The president of the propane vendor was also interviewed. The Division of State Audit obtained daily base price information from the Purchasing Division of the Department of General Services. Based on that pricing information, calculations were performed to determine the prices the vendor should have billed the Department of Environment and Conservation. The Division of State Audit also performed a similar review of propane purchases at Tims Ford State Park (the only other state park with a propane tank large enough for the cost-saving feature in the contract to be an issue).

Background

In May 2002, Fall Creek Falls State Park staff filed a complaint with the Purchasing Division, Department of General Services, for deliveries made by the propane vendor in February 2002. The complaint indicated that the park received six invoices for a total of 8,315.7 gallons for the period February 12-15, 2002, and paid \$6,116.05. The complaint further

indicated that if the park had received the entire 8,315.7 gallons in one delivery, the price would have been only \$3,663.90, a savings of \$2,452.15 for that week.

Purchasing Division staff contacted the vendor, and the vendor agreed to credit the overpayment identified by the park staff by foregoing state payment to him for four submitted but unpaid invoices totaling \$5,365.94. The vendor's proposal was accepted by the Purchasing Division on June 5, 2002.

Subsequently, park staff conducted further review of the vendor's invoices and identified additional periods in which cost savings would have been realized had the vendor made one large delivery instead of multiple smaller deliveries. Although park staff identified other opportunities for savings, they did not file a formal complaint with the Purchasing Division because discussions had already been initiated with the appropriate staff of the Department of General Services regarding the multiple smaller deliveries from the vendor.

A meeting on the additional multiple deliveries occurred between staffs of the Department of Environment and Conservation and the Department of General Services in August 2002, but the matter was not pursued further because General Services staff determined that a large portion of lost cost-savings was the result of the improper ordering and monitoring of propane by park staff and management. Subsequently, the matter came to the attention of the Enforcement Division of the Attorney General's Office, which referred it to the Division of State Audit.

Details of the Review

From the invoices reviewed by the Division of State Audit, it appears that in the beginning of the contract (September and October 1999) the vendor delivered several large loads and charged the park with the appropriate markup except on one occasion. The initial deliveries with the appropriate markup enabled the park to realize the cost-savings envisioned by the contract's pricing structure. The vendor stopped making the larger deliveries on November 15, 1999, for reasons unknown and started making smaller multiple deliveries. From interviews with the vendor, the reason for the change from larger deliveries to frequent smaller deliveries was due to the non-functioning fuel valves at the park that were incapable of receiving propane from the larger transport trucks. The vendor did not recall making any deliveries with the larger transport trucks. The certified metered delivery readings on the invoices show that deliveries over 5,000 gallons were in fact made at the beginning of the contract by the vendor but ceased in November 1999. The park management and staff did not recall when the fuel valves stopped functioning and whether the smaller deliveries resulted thereafter. They stated that the park had been receiving deliveries from the larger transport trucks, either from the vendor or under the previous contract with the prior vendor. From November 15, 1999, through June 30, 2002, the vendor made 13 smaller deliveries during a week's period that could have been consolidated into larger deliveries. On these 13 occasions, the state was charged the higher markup. The contract with this vendor to deliver propane to this park (for this particular county) lapsed at the end of

June 2002. No problems were noted for Fall Creek Falls in regard to deliveries from the subsequent vendor after June 2002.

Because of potential problems with propane deliveries to other state parks, the Division of State Audit expanded its scope and determined that one other park, Tims Ford State Park, located in Franklin County also housed a large-capacity storage tank. It was also determined that the propane delivered to Tims Ford State Park was from the same vendor. From December 2000 through January 2004, the vendor made seven smaller deliveries during a week's period that could have been consolidated into larger deliveries. On these seven occasions, the state was charged the higher markup.

This review determined that the vendor did not intentionally make smaller deliveries to Fall Creek Falls State Park or Tims Ford State Park in order to charge the state the higher markup. With the non-functioning fuel valves at Fall Creek Falls State Park and park staff's failure to properly place orders with the vendor, it does not appear that the vendor was at fault. In the case of Tims Ford State Park, it also appears that park staff failed to properly place orders for larger deliveries with the vendor. It appears that staff at both parks totally relied on the vendor for the quantities delivered without specifying larger deliveries. Therefore, the vendor's preference to make multiple deliveries with smaller-load trucks resulted in lost cost-savings. Staff from both parks stated that they were not aware of the contract's cost-saving provision for larger deliveries, and therefore, the relative quantities of individual propane deliveries had not been an issue. This review also determined other deficiencies in the procurement of propane at both parks.

16. Lack of oversight on propane purchases resulted in lost cost-savings

Finding

The lack of proper oversight at Fall Creek Falls State Park and Tims Ford State Park resulted in the parks paying considerably more for propane than was necessary. The combined cost-savings lost from the lack of proper oversight and the multiple small deliveries for both Fall Creek Falls for the period November 1999 through June 2002 and Tims Ford state parks for the period December 2000 through January 2004 was \$36,795 (\$23,737 and \$13,058, respectively).

Proper oversight of propane purchases from a statewide contract would, at a minimum, include obtaining a copy of the contract, reading the contract, and contacting the Department of General Services for answers to any questions a procurement officer might have regarding the contract. This particular statewide contract with the propane vendor expressly specified a lesser markup for deliveries of 5,000 gallons or more. In fact, there was a separate contract line for smaller deliveries and one for those of 5,000 gallons or more. Had staff from either park obtained a copy of the contract, they would have been aware of the provisions for the cost-savings for deliveries of 5,000 gallons or more.

Without the knowledge of the contract provisions, the parks' staff and management did not make a concerted effort to direct the vendor's deliveries. Management at Fall Creek Falls State Park instructed the vendor to make deliveries so that the park would not run out of propane. Furthermore, management did not ensure that non-functioning valves were repaired in a timely manner because there were no safety issues, and management was not aware that there was a cost-savings associated with properly functioning valves.

With proper attention afforded the contract provisions, park staff should have called the vendor and ordered a specific amount of propane, according to the parks' needs and budget. At Fall Creek Falls State Park, staff left the decision of the amount of gas to be delivered and delivery times to the vendor. Tims Ford State Park staff monitored the propane meter at the park and called the vendor to make a delivery when the park's tank capacity was low. However, the park's staff ordered the propane without specifying a minimum amount to be delivered.

With the volatility of propane prices, proper oversight would also include park staff verifying the propane price per gallon with the Department of General Services or one of the main propane distribution terminals. Neither staff nor management from either park verified the daily prices that the vendor charged. However, auditor review of the relevant prices indicated only minor deviations from market prices.

Proper monitoring of deliveries would also be an important part of the oversight function for propane deliveries. Amounts of propane delivered should have been verified through independent means by park staff. Park staff at Fall Creek Falls State Park stated they were not physically present at the storage tanks when deliveries were made. Random readings of the storage tanks were taken according to park staff. At Tims Ford State Park, staff stated that they were physically present at the storage tank to monitor the deliveries.

It should also be noted that in June 2001, the General Assembly amended Section 11-3-112, *Tennessee Code Annotated*, and authorized the Department of Environment and Conservation to develop a method of purchasing raw materials, merchandise for resale, supplies, and equipment necessary for providing quality services for state park operations without the approval of any other agency of state government. The department's new purchasing policies and procedures for state parks (Policy Number 1, Section VI. G.) reserve the right not to buy off the statewide contracts if lower pricing is available elsewhere. The recommendations below were made with consideration given to these new purchasing policies.

Recommendations

Department of Environment and Conservation management should review the propane needs of all parks and determine the most efficient and cost-effective method for purchasing propane, whether by statewide contract or otherwise. Regardless of whether the department utilizes a statewide contract or not, the department should ensure the parks have proper oversight of propane purchases.

1. Department of Environment and Conservation management should ensure that procurement personnel have appropriate knowledge of contract terms and conditions, as well as department policies and procedures related to propane purchases.
2. Department of Environment and Conservation management should ensure that appropriate written policies and procedures are established and implemented pertaining to ordering propane, monitoring propane deliveries, verifying the amounts delivered, and confirming propane market prices.
3. Department of Environment and Conservation management should use this situation as a starting point to review other possible procurement issues. The review should be appropriately documented. Management should promptly advise its own internal audit section and the Division of State Audit regarding any issues noted by management.
4. Propane purchases should be routinely monitored by park management for frequency, accuracy, and reasonableness. Propane purchases should also be periodically reviewed by internal audit. Park management should ensure that park staff physically observe deliveries and independently verify amounts delivered.
5. The correct tank capacity at each facility should be reflected on the statewide propane contract. Our review revealed that the statewide propane contract listed incorrect tank capacity for two parks.
6. Park management should make sure that equipment is working, and if not, the equipment should be promptly repaired.
7. Department of Environment and Conservation management should ensure that the appropriate staff at the parks are properly trained to use TOPS if a statewide contract is utilized.
8. Department of Environment and Conservation management should ensure that complaints are appropriately submitted to the Department of General Services so that the two departments can pursue reasonable resolution of the issues in a timely manner.

Management's Comment

We concur. Park management did not fully understand all of the terms and conditions included in the propane contract. Area management staff will review the propane needs of all parks and determine the most efficient and cost-effective method for purchasing propane, whether by statewide contract or otherwise. Better oversight through the area manager system and through a more comprehensive training program that specifically addresses propane purchases should give managers a better understanding of the propane contract. The area

manager's operational reviews will ensure that proper monitoring of propane deliveries and inventories is ongoing.

OBSERVATIONS AND COMMENTS

TITLE VI OF THE CIVIL RIGHTS ACT OF 1964

Section 4-21-901, *Tennessee Code Annotated*, requires each state governmental entity subject to the requirements of Title VI of the Civil Rights Act of 1964 to submit an annual Title VI compliance report and implementation plan to the Department of Audit by June 30 each year. The Department of Environment and Conservation filed its compliance reports and implementation plans on June 30, 2003, and June 28, 2002.

Title VI of the Civil Rights Act of 1964 is a federal law. The act requires all state agencies receiving federal money to develop and implement plans to ensure that no person shall, on the grounds of race, color, or origin, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving federal funds. The Tennessee Title VI Compliance Commission is responsible for monitoring and enforcement of Title VI. A summary of the dates state agencies filed their annual Title VI compliance reports and implementation plans is presented in the special report *Submission of Title VI Implementation Plans*, issued annually by the Comptroller of the Treasury.

APPENDIX

ALLOTMENT CODES

327.01	Administrative Services
327.03	Conservation Administration
327.04	Historical Commission
327.06	Land and Water Conservation Fund
327.08	Archaeology
327.11	Geology
327.12	Tennessee State Parks
327.14	Natural Heritage
327.15	Tennessee State Parks Maintenance
327.17	Tennessee Elk River Resources Management
327.18	Maintenance of Historic Sites
327.19	Local Parks Acquisition Fund
327.20	State Lands Acquisition Fund
327.22	State Lands Acquisition Compensation

327.23 Used Oil Collection Program
327.24 West Tennessee River Basin Authority Maintenance
327.26 West Tennessee River Basin Authority
327.28 Tennessee Dry Cleaners Environmental Response Fund
327.30 Environment Administration
327.31 Air Pollution Control
327.32 Radiological Health
327.33 Community Assistance
327.34 Water Pollution Control
327.35 Solid Waste Management
327.36 Department of Energy Environmental Oversight
327.37 Abandoned Lands Program
327.38 Hazardous Waste Remedial Action Fund
327.39 Water Supply
327.40 Groundwater Protection
327.41 Underground Storage Tanks
327.42 Solid Waste Assistance Fund
327.43 Environmental Protection Fund
327.95 Duck River Water Infrastructure Fund