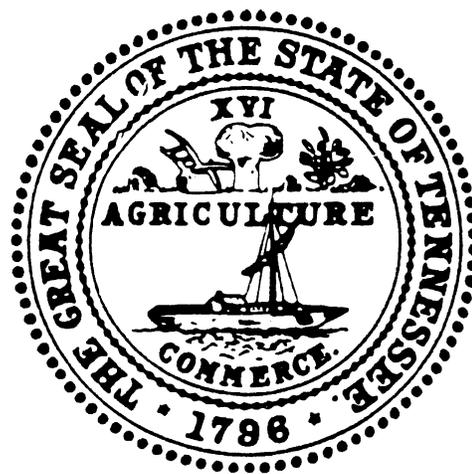


AUDIT REPORT

Tennessee Commission on Aging and Disability

February 2006



STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY

Department of Audit
Division of State Audit



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

February 28, 2006

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

The Honorable Nancy Peace, Executive Director
Tennessee Commission on Aging and Disability
Suite 825, Andrew Jackson State Office Building
Nashville, Tennessee 37243

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Tennessee Commission on Aging and Disability for the period July 1, 2001, through May 31, 2005.

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/cj
05/077



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

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June 10, 2005

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 Tennessee Commission on Aging and Disability for the period July 1, 2001, through May 31, 2005.

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 Tennessee Commission on Aging and Disability's compliance with laws, regulations, and provisions of contracts or grant agreements significant to the audit objectives. Management of the Tennessee Commission on Aging and Disability 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 commission'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 commission's internal control and/or instances of noncompliance to the commission's management in a separate letter.

Sincerely,

Arthur A. Hayes, Jr., CPA
Director

AAH/cj

State of Tennessee

Audit Highlights

Comptroller of the Treasury

Division of State Audit

Financial and Compliance Audit
Tennessee Commission on Aging and Disability
February 2006

AUDIT SCOPE

We have audited the Tennessee Commission on Aging and Disability for the period July 1, 2001, through May 31, 2005. 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 conflicts of interest, computer applications access, equipment, Area Agency monitoring, compliance with Policy 20 of the Department of Finance and Administration, supplemental payroll, 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.

AUDIT FINDINGS

The Commission's Management Has Not Obtained Adequate Assurances About the Security of Information in the Social Assistance Management System, Has Not Properly Monitored Access to the Information at the Area Agency Level, and Did Not Mitigate the Risk of Improper Access, Alteration, and Theft of Data in the System

The commission has no written agreement with the system provider and has not required the system provider to furnish the commission with independent assurances that client information is adequately protected. The commission has not adequately monitored access to the system (page 6).

The Commission's Management Did Not Adequately Monitor Its Area Agencies' Compliance With the Terms of Their Grant Agreements, and Did Not Mitigate the Risk of Noncompliance and Inadequate Performance of Services for the Elderly and Disabled

Since July 1, 2001, only three of the nine Area Agencies have been monitored. The invoices for reimbursement submitted by the Area Agencies do not have enough supporting documentation for the commission to verify the accuracy of the information on the invoices. The commission has not been routinely reviewing the annual Single Audit Reports obtained by the Area Agencies (page 10).

The Commission's Management Did Not Comply With the Provisions of the Department of Finance and Administration's Policy Concerning Grants Accounting and Did Not Mitigate the Risk of Inaccurate Reporting to Its Grantors

The commission did not load all of its federal grants onto the State of Tennessee Accounting and Reporting System (STARS) Grant Control

Table, did not record the federal grant award amounts in the STARS Grant File, did not draw federal funds using the STARS Daily Grant Drawdown Report, did not use the STARS "Schedule of Grant Activity" report as the basis for preparing the Schedule of Expenditures of Federal Awards, and did not use the STARS grants module reports to prepare its Federal Financial Status Reports (page 15).

Financial and Compliance Audit Tennessee Commission on Aging and Disability

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Financial and Compliance Audit Tennessee Commission on Aging and Disability

INTRODUCTION

POST-AUDIT AUTHORITY

This is the report on the financial and compliance audit of the Tennessee Commission on Aging and Disability. 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.”

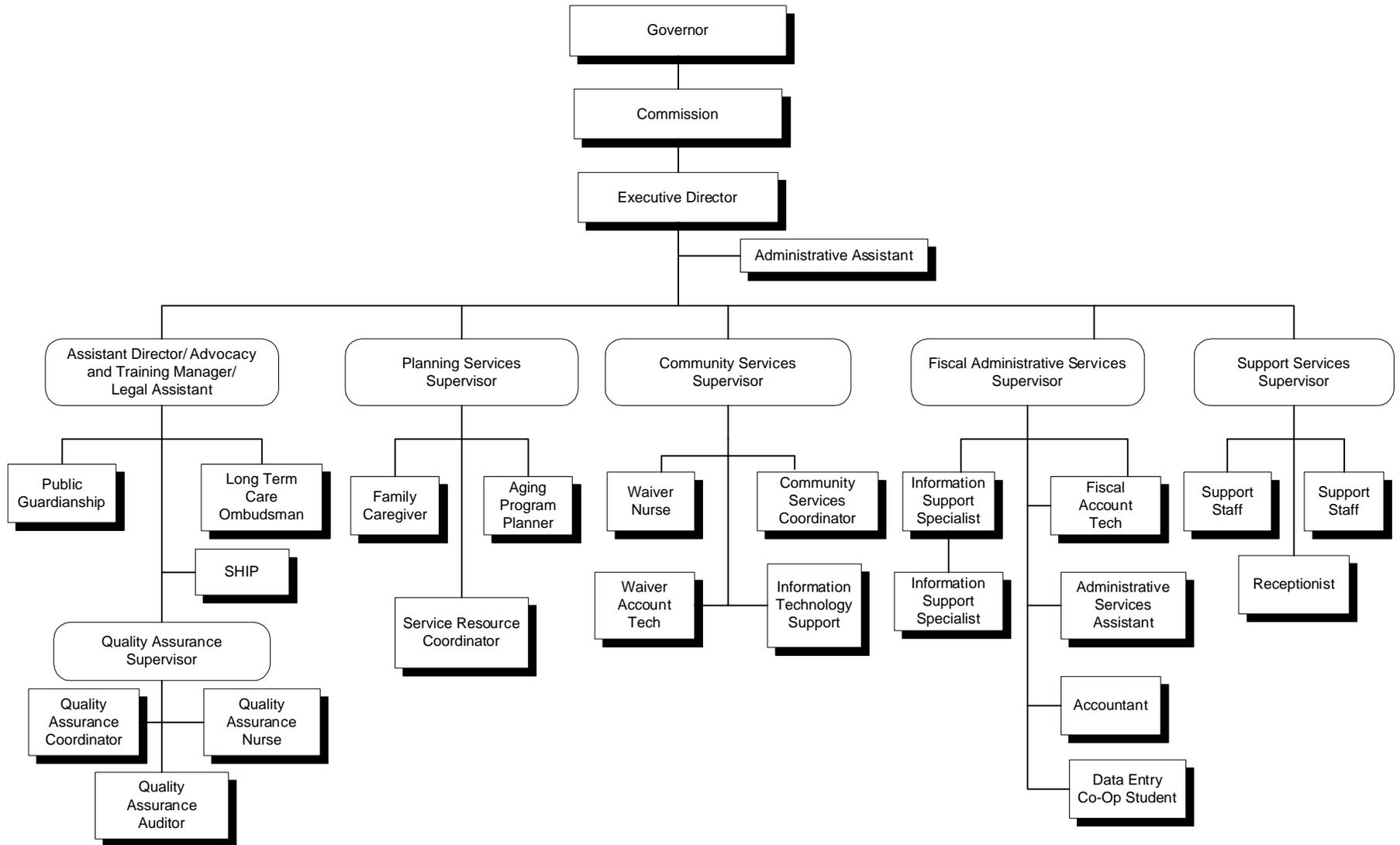
Section 8-4-109, *Tennessee Code Annotated*, authorizes the Comptroller of the Treasury to audit any books and records of any governmental entity that handles public funds when the Comptroller considers an audit to be necessary or appropriate.

BACKGROUND

The Commission on Aging and Disability, currently authorized under Section 71-2-101, *Tennessee Code Annotated*, was created by the General Assembly in 1963 and is designated as the state agency on aging by the Governor. As the state agency on aging, the commission is mandated by the Older Americans Act [42 U.S.C.A. 3001] to provide leadership relative to all aging issues on behalf of older persons in the state, and is the focal point for aging issues and the advocate within state government for older Tennesseans. The commission serves as a clearinghouse for information on needs characteristic of older Tennesseans and of adults with disabilities needing home and community services. In addition to responding to requests for information, in 2001 the commission’s responsibilities were expanded to include planning, coordinating, and implementing home- and community-based long-term care services for adults with disabilities. The commission consists of 18 members appointed by the Governor: 2 members from the General Assembly; the commissioners of Health, Human Services, Veterans Affairs, and Mental Health and Developmental Disabilities; the Council on Developmental Disabilities Executive Director; and a representative of the Governor’s office. Approximately 95% of the commission’s expenditures go to nine Area Agencies across the state designated by the commission to plan for and provide services to older Tennesseans and adults with disabilities.

An organization chart of the Tennessee Commission on Aging and Disability is on the following page.

TENNESSEE COMMISSION ON AGING AND DISABILITY ORGANIZATION CHART



AUDIT SCOPE

We have audited the Tennessee Commission on Aging and Disability for the period July 1, 2001, through May 31, 2005. 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 conflicts of interest, computer applications access, equipment, Area Agency monitoring, compliance with Policy 20 of the Department of Finance and Administration, supplemental payroll, 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 FINDING

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 Tennessee Commission on Aging and Disability filed its report with the Department of Audit on December 12, 2002, 11 days late. A follow-up of the prior audit finding was conducted as part of the current audit.

RESOLVED AUDIT FINDING

The current audit disclosed that the Tennessee Commission on Aging and Disability has corrected the previous audit finding concerning its failure to submit the annual Financial Integrity Act responsibility letter.

OBJECTIVES, METHODOLOGIES, AND CONCLUSIONS

CONFLICTS OF INTEREST

Our objectives consisted of determining whether

- management is aware of the executive orders, state statutes, and state regulations that have requirements concerning conflicts of interest and has adequate procedures in place to ensure compliance, and
- the commission has complied with the applicable executive orders, state statutes, and state regulations.

We met with management to gain an understanding of management's knowledge of the pertinent laws, statutes, and regulations and procedures that it had in place to ensure compliance. We then requested signed conflict-of-interest statements for each current commission member and all employees that had responsibilities which would make conflicts of interest an issue. We then reviewed the statements to determine if they contained the proper wording and were signed.

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

- management is aware of the executive orders, state statutes, and state regulations that have requirements concerning conflicts of interest and has adequate procedures in place to ensure compliance; and
- the commission has complied with the applicable executive orders, state statutes, and state regulations.

COMPUTER APPLICATIONS ACCESS

Our objectives consisted of determining whether

- the procedures described by management to limit access to only those employees who need the access and not create inadequate segregation of duties were adequate;
- access to the State of Tennessee Accounting and Reporting System (STARS) was limited to active employees whose job duties required the access and the access did not create an inadequate segregation of duties;
- access to the State Employee Information System (SEIS) was limited to active employees whose job duties required the access and the access did not create an inadequate segregation of duties;

- access to the Tennessee On-Line Purchasing System (TOPS) was limited to active employees whose job duties required the access and the access did not create an inadequate segregation of duties;
- access to the Property of the State of Tennessee (POST) was limited to active employees whose job duties required the access and the access did not create an inadequate segregation of duties;
- access to the Social Assistance Management Systems (SAMS) was limited to active employees whose job duties required the access and the access did not create an inadequate segregation of duties; and
- the commission obtained adequate assurances from the SAMS provider that the client information in the system was protected.

We met with management to gain an understanding of the procedures that were being used to limit access for these computer applications to only those employees whose job duties require it while at the same time not creating inadequate segregation of duties. Since SAMS is used only by this commission, we discussed with management the purpose and uses of this system, the organizations across the state that use it, the controls in place to limit access to only those persons whose job duties require it, and the agreements that the commission has with Synergy, the SAMS provider, about client information protection. We obtained from the Department of Finance and Administration a current listing of those employees who had access to STARS and the payroll side of SEIS. We obtained from the Department of General Services a current listing of employees who had access to TOPS and POST. We obtained from the Department of Personnel a current listing of employees with access to the personnel side of SEIS. We obtained from commission management a current listing of persons across the state who had access to SAMS. For each employee with access to STARS, SEIS, TOPS, and POST, we determined if the person was an active employee as of the date of the listing, had job duties that required the authorized level of access, and the level of access did not create an inadequate segregation of duties. Because of the large number of persons who had access to SAMS, we selected a random sample and determined for each person in the sample if the person was an active employee as of the date of the listing, had job duties that required their authorized level of access, and had a level of access that did not create an inadequate segregation of duties.

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

- access to STARS was limited to active employees whose job duties required the access and access did not create an inadequate segregation of duties;
- access to SEIS was limited to active employees whose job duties required the access and the access did not create an inadequate segregation of duties;
- access to TOPS was limited to active employees whose job duties required the access and the access did not create an inadequate segregation of duties; and
- access to POST was limited to active employees whose job duties required the access and the access did not create an inadequate segregation of duties.

However, we also found that

- access to SAMS was not always limited to active employees whose job duties required the access, although the access did not create an inadequate segregation of duties;
- the commission did not obtain adequate assurances from the SAMS provider that the client information in the system was protected; and
- the procedures described by management were not adequate for access to SAMS.

These problems are discussed in Finding 1.

1. The commission's management has not obtained adequate assurances about the security of information in the Social Assistance Management System, has not properly monitored access to the information at the Area Agency level, and did not mitigate the risk of improper access, alteration, and theft of data in the system

Finding

The commission has not required the company which operates the web-based Social Assistance Management System (SAMS) database of client information to obtain and provide to the commission third-party assurances about the safety of the client information.

The SAMS system is a web-based interactive database owned by Synergy, Inc., that contains all pertinent personal information on clients served by the various Senior Adult programs overseen by the commission. This includes social security numbers; home addresses; and demographic information such as gender, ethnicity, income level, disabilities, and programs in which each client participates. This database is used by both the commission and the nine local Area Agencies. These nine agencies are part of a state-wide network of quasi-governmental organizations which carry out services for the aged that are funded in part through grants from the commission. The database server is located in Essex Junction, Vermont, and is under the control of Synergy. The commission does not have an agreement with Synergy, although all of the Area Agencies do. None of the agreements require Synergy to obtain an independent audit of the safety of the information in this computer network or to provide documentation that Synergy has an adequate disaster recovery plan. The sensitive nature of the information on each client and the lack of direct control over the facility and staff where the information is stored make such assurances critically important. Further, the system does not have documentation that would permit the commission and the Area Agencies to know when information in the system has been changed or deleted.

The commission has not properly monitored the degree to which the Area Agencies limit access to the client information. In a sample of 25 active usernames, one (4%) was assigned to a person who no longer worked at the Area Agency. Two usernames (8%) were not assigned to a specific person. Of the 22 in the sample that were assigned to active employees, three of the employees (14%) did not have job duties that required access. One of these three is a

commission employee. In addition, there were five other commission employees who had varying levels of access to SAMS but did not need it.

Recommendation

The Executive Director should immediately contact Synergy and begin work on an agreement which would spell out the responsibilities of each. At a minimum, the agreement should require Synergy to obtain an annual data integrity audit, which would include an evaluation of Synergy's disaster-recovery plan.

The Assistant Director should draft procedures for all Area Agencies which include limiting access to only those persons whose job duties require it. Unused usernames should be revoked. Assigned usernames should be specific to individual users. Access to SAMS should be revoked the same day that an employee leaves employment or no longer requires the access.

The Executive Director should request that Synergy create an access level for commission employees who have administrator access which would not permit them to be able to delete any information. Synergy should also be asked to develop documentation that could be used by administrators to determine the user who made a particular change in the database. In addition, management should independently ensure that other risks are adequately identified and assessed and that effective mitigating controls are designed and implemented.

Management's Comment

We concur.

The Tennessee Commission on Aging and Disability (TCAD) has requested Synergy to address the system being able to determine when client data has been changed and by whom such changes have been made. Synergy has informed TCAD that this issue will be addressed with a future systems enhancement.

The TCAD has contacted the Administration on Aging and another state unit on aging concerning active contracts these agencies have with Synergy. The Commission is planning to review, reverse and develop contracts with Synergy based upon the requested documents from federal and state agencies and the Synergy license agreement.

The TCAD staff have performed a desk audit on all active usernames in the Social Assistance Management System (SAMS) for the purpose of determining the proper access for each user being correctly identified. As a result of the recommendation of the audit, TCAD staff no longer have the ability to write or delete information contained in client files. TCAD staff continue to have the ability to read client files.

TCAD staff responsible for Information Technology (IT) are in the process of drafting procedures for all area agencies on aging and disability to comply with the recommendation including:

- Limiting the number of staff having access to SAMS;
- Implementing procedures for revoking staff access to SAMS upon termination of employment or change in job responsibilities.

TCAD staff are developing a protocol to implement monitoring of data integrity and data security in relationship to SAMS at the state and local levels.

EQUIPMENT

Our objectives consisted of determining whether

- the procedures described by management to account for and safeguard equipment were adequate;
- all equipment acquired before April 2004 was inventoried by June 30, 2004;
- the department's property and equipment as listed in the Property of the State of Tennessee (POST) system represented an accurate and complete listing of equipment on hand;
- the department was maintaining proper accountability over the vehicle that was assigned to it;
- additions to POST since July 1, 2001, reconciled to expenditures charged to equipment in the State of Tennessee Accounting and Reporting System (STARS) during the same period; and
- lost or stolen equipment was properly reported to the Office of the Comptroller and deleted from POST.

We interviewed key personnel to gain an understanding of the procedures used to account for and safeguard equipment and then assessed the adequacy of the procedures. We obtained from the Department of General Services a current listing of all equipment assigned to the commission. We determined if all equipment with an acquisition date before April 2004 had an inventory date in POST between April 2004 and June 30, 2004. We tested the 25 costliest pieces of equipment to determine if the equipment could be located and the information about the equipment in POST was accurate. Using this same listing, we identified all equipment that had an acquisition date since July 1, 2001. We obtained from State Audit's Information Systems section a schedule of all expenditures charged to equipment in STARS and determined if the total of these expenditures would reconcile to the total in POST of equipment with an acquisition date during the same time period. We obtained from State Audit's correspondence file a list of

equipment reported as lost or stolen since July 1, 2002, and determined if the equipment was properly reported to the Office of the Comptroller and deleted from POST.

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

- the procedures described by management to account for and safeguard equipment were adequate;
- all equipment acquired before April 2004 was inventoried by June 30, 2004;
- the department's property and equipment as listed in the POST system represented an accurate and complete listing of equipment on hand;
- the department was maintaining proper accountability over the vehicle that was assigned to it;
- additions to POST since July 1, 2001, reconciled to expenditures charged to equipment in STARS during the same period; and
- lost or stolen equipment was properly reported to the Office of the Comptroller and deleted from POST.

AREA AGENCY MONITORING

Our objectives consisted of determining whether

- management has procedures in place which ensure that its Area Agencies are adequately monitored;
- management has documented its reviews of the Area Agencies' annual Single Audit Reports;
- management followed up on findings shown in Single Audit Reports and monitoring reports to ensure that the conditions described in the findings have been corrected;
- if any monitoring reports were issued by the commission, the testwork in the related monitoring working papers supported the conclusions expressed in the monitoring reports; and
- expenditures charged to the Area Agencies agreed or reconciled to invoices for reimbursement, and the expenditures shown on the invoice complied with the terms of the contract.

We met with management and discussed the procedures used to ensure that the Area Agencies are adequately monitored. We obtained from the Municipal Audit Division of the Comptroller of Treasury the Area Agencies' annual Single Audit Reports issued for periods beginning July 1, 2001, through the most recent audit period to determine if any had findings related to the programs funded by the commission. We then asked commission management for documentation showing that it had followed up to determine if the appropriate remedial actions

had been taken. Three of the nine Area Agencies had been monitored during the audit period. This was done by the Department of Finance and Administration (F&A). We obtained a copy of the monitoring reports from F&A; two had findings. We then asked management for documentation of its follow-up to determine if appropriate corrective action had been taken. The commission did not conduct any formal monitoring of its own during the audit period; so there were no monitoring working papers to review. We obtained from State Audit's Information Systems section a listing of all expenditures charged to grants and subsidies during the audit period. From this listing, we tested a sample to determine if the expenditure amounts could be agreed or reconciled to the invoices for reimbursement submitted by the Area Agencies in the sample, and the expenditures on the invoices complied with the terms of the contract.

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

- management did not have adequate procedures in place which ensure that its Area Agencies are adequately monitored,
- management did not document its reviews of the Area Agencies' annual Single Audit Reports,
- management did not document follow-up that may have been done on findings shown in Single Audit Reports and monitoring reports to ensure that the conditions described in the findings have been corrected, and
- expenditures charged to the Area Agencies agreed or reconciled to invoices for reimbursement, but we could not determine if the expenditures complied with the terms of the contract because the invoices contained only program totals.

The problems noted above are discussed further in Finding 2.

2. The commission's management did not adequately monitor its Area Agencies' compliance with the terms of their grant agreements, and did not mitigate the risk of noncompliance and inadequate performance of services for the elderly and disabled

Finding

The Tennessee Commission on Aging and Disability has grant contracts with the nine local Area Agencies. These nine agencies are part of a state-wide network of quasi-governmental organizations that have been designated to plan for and provide services to older Tennesseans and adults with disabilities. Since July 1, 2001, six of the nine Area Agencies have not been formally monitored to determine compliance with their grant agreements and whether the information on their invoices for reimbursement was accurate. During this period, the commission spent approximately \$31 million per fiscal year on grants to the Area Agencies, or more than 95% of the commission's total expenditures.

Each Area Agency has a five-year agreement with the commission which began July 1, 2001. The Area Agencies submit invoices each month and are paid based on their estimate of the next month's expenditures.

Each agreement states the following:

The grantee shall be compensated for actual, reasonable, and necessary costs based upon the Grant Budget, not to exceed the maximum liability established in Section C.1. Upon progress toward the completion of the work, as described in Section A of the Grant, the Grantee shall submit invoices, in form and substance acceptable to the State, with all of the necessary documentation, prior to any reimbursement of allowable costs.

Although the agencies obtain annual Single Audits from public accountants, these reports are not received until at least six months after the end of the agency's fiscal year. These reports provide useful information as to whether an agency has complied with laws and regulations governing the financial assistance expended. However, they do not provide the timely ongoing assurances of compliance and performance that regular contact and site visits provide. Furthermore, the commission has not been routinely reviewing annual Single Audit reports and following up on the corrective action taken by the agencies to correct the findings contained in these reports.

Office of Management and Budget Circular A-133, Subpart D ____400 (d), states, "A pass-through entity shall perform the following for the Federal awards it makes . . . (3) Monitor the activities of subrecipients as necessary to ensure that Federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved."

By not conducting regular monitoring visits to the Area Agencies, there is a greater risk that federal awards could be spent on unallowable activities, the Area Agencies could have unallowable costs, and the Area Agencies could fail to provide the necessary program matching funds; and these instances of noncompliance would not be detected timely.

Recommendation

The Executive Director should immediately direct her staff to draft an up-to-date monitoring guide which includes all key compliance features of the commission's programs awarded to the Area Agencies. The Assistant Director should make visits with his staff to the Area Agencies, monitoring both programmatic and fiscal activities. The Assistant Director should also set up a log for the annual audit reports of the Area Agencies. The log should include the date that a report is received, the date that it is reviewed, a description of any findings which relate to programs being funded by the commission, the date that the commission contacted the Area Agency about correcting the findings, and the date of any follow-up to determine if the necessary corrective action has been taken. Management should ensure that all risks of subrecipient noncompliance, including these noted in this finding, are adequately

identified and assessed and that effective mitigating controls are designed and implemented. These controls should include ongoing monitoring for compliance with all pertinent requirements. Once the commission's audit committee is established, it should review and approve management's risk assessment.

Management's Comment

We concur.

The Commission is committed to improving its contract monitoring to ensure that it reduces the risks of noncompliance and inadequate performance. Below are the circumstances related to the finding and the actions taken to address the shortcomings.

PAR (Program Accountability and Review) monitored contracts for the Commission for several years. However, the last time PAR monitored an area agency on aging and disability (area agency) was in May 2002.

The Commission resumed monitoring responsibilities and employed a program coordinator and a quality assurance nurse in 2003. This occurred around the same time the Commission implemented the TennCare Waiver for Home and Community-Based Services. The nurse's role was to conduct quality assurance monitoring of Waiver case management providers. In FY04, the nurse conducted eleven (11) monitoring site visits (five were area agencies, three were independent case management providers, and three were services providers). Although the quality assurance nurse reviewed five area agencies' waiver functions, the nurse did not review the other area agency programs or financial matters. The quality assurance program coordinators did not monitor any contractors.

In November 2004, the Commission hired a quality assurance supervisor. The supervisor's first priority was to write a quality assurance manual for the TennCare Waiver program. The Commission had not reviewed or revised its monitoring tools for reviewing area agencies since 1997, so the supervisor coordinated the review, revision, and standardization of all the monitoring tools used by the area agencies to review their contractors. In addition to reviewing and reversing the Title III monitoring tools, the supervisor has also designed monitoring tools used by the Commission when reviewing area agencies and independent case management contractors in regard to the TennCare Waiver functions.

The Commission hired an auditor for the quality assurance unit in March 2005 and replaced the program coordinator in November 2005.

The Commission has implemented a schedule for annually monitoring the area agencies. The quality assurance unit conducted the annual assessment and review of: 1) the South Central Area Agency on Aging and Disability in May and August 2005; 2) the Upper Cumberland Area Agency on Aging and Disability in July and August 2005; 3) the North Area Agency on Aging and Disability in November 2005. The quality assurance unit will conduct site visits to Greater

Nashville Regional Council in January 2006. The remaining Area Agencies will be scheduled in this order: Memphis, East Tennessee, First Tennessee, and Southeast Tennessee.

The Quality Assurance supervisor has developed a tracking log that shows a list of the agencies, the date of the site visit, the date the report was sent to the agency, the date the plan of correction was submitted, and the date that the plan of correction was accepted.

The Division of Resource Development and Support has approved the Commission's FY 2006 Sub-recipient Monitoring Plan, as required by the Department of Finance and Administration, Policy Statement 22, *Sub-recipient Monitoring*.

The Quality Assurance unit only has one auditor. He does not have any state government experience. To ensure that this employee receives appropriate guidance and training, the supervisor has requested assistance from two sources: 1) Resource Development and Support, and 2) the Department of Mental Health and Development Disabilities (which also has a TennCare Waiver). With the requested guidance, unit staff believe that they will be able to adequately meet the requirements.

COMPLIANCE WITH POLICY 20 OF THE DEPARTMENT OF FINANCE AND ADMINISTRATION

The Department of Finance and Administration's (F&A) Policy 20, *Recording of Federal Grant Expenditures and Revenues*, was first issued in April 1991. It was revised in February 2000.

The policy's introduction states that it was issued in order to

- A. Establish effective cash management procedures for Federal programs to maximize State resources.
- B. Fulfill the requirements established by the federal Cash Management Improvement Act of 1990.
- C. Define uniform procedures to be applied by all agencies to ensure accurate accounting and reporting of the financial activity of federal programs.

Approximately 70% of the commission's expenditures are federally funded. Paragraph 3 of the policy states, "All State departments and agencies . . . must be in full compliance by July 1, 2000."

Our objectives consisted of determining whether

- management understands the requirements of Policy 20 and has procedures in place to ensure compliance,
- management has loaded all of the key information on its federal grants onto the State of Tennessee Accounting and Reporting System (STARS) Grant Control Table,

- management has recorded federal grant awards in the STARS Grant Control Table not later than the end of the month in which the grant award notification has been received from the federal government,
- the amounts shown on the commission's Schedule of Expenditures of Federal Awards reconcile to the amounts shown on the STARS Schedule of Grant Activity,
- federal draws reconcile to the STARS Daily Drawdown Report, and
- the information on the commission's most recent Title III Federal Financial Status Report reconciles to the STARS Schedule of Grant Activity.

We asked management about their understanding of F&A Policy 20 and the procedures used to comply with requirements of the policy. Management stated that it was not following Policy 20. Management said that it had loaded some key information on federal grants on the STARS Grant Control Table, but it had not entered the federal grant awards amounts. We obtained and reviewed the applicable STARS reports for the fiscal year ended June 30, 2004, to determine the extent to which information on its federal grants had been loaded on the STARS Grant Control Table. We obtained the commission's Schedule of Expenditures of Federal Awards (SEFA) for the fiscal year ended June 30, 2004, and were told that no attempt had been made to reconcile the amounts on it to the STARS Schedule of Grant Activity. Management did state that it had reconciled the amounts to another STARS report that was not part of the STARS grant module. We reviewed the documentation to determine if the reconciling items were proper. Management told us that it did not use the STARS Daily Drawdown Reports to determine the amount of the draws. Nevertheless, we obtained the documentation on all federal draws made during the fiscal year ended June 30, 2004, and determined if the draw amounts could be reconciled to the information on the invoices for reimbursement submitted by the Area Agencies. We obtained from management the semi-annual Federal Financial Status Report due September 30, 2004, for the Title III program and were told that management did not use the STARS grant module reports to prepare the report and did not reconcile the information on the report to STARS.

Based on our discussions with management and the subsequent testwork, we concluded that

- management did not have procedures in place to ensure compliance with the provisions of Policy 20,
- management had not loaded all of the key information on its federal grants onto the STARS Grant Control Table,
- management had not recorded any federal grant awards in the STARS Grant Control Table,
- the amounts shown on the commission's Schedule of Expenditures of Federal Awards did not reconcile to the amounts shown on the STARS Schedule of Grant Activity,
- federal draws did not reconcile to the STARS Daily Drawdown Report, and

- the information on the commission’s most recent Title III Federal Financial Status Report did not reconcile to the STARS Schedule of Grant Activity.

This is discussed further in Finding 3.

3. The commission’s management did not comply with the provisions of the Department of Finance and Administration’s policy concerning grants accounting and did not mitigate the risk of inaccurate reporting to its grantors

Finding

The commission did not enter all of its grants on the STARS Grant Control Table; did not enter federal grant awards in the STARS Grant Table; and did not use the STARS grant module reports to calculate its federal drawdowns, and prepare the Schedule of Expenditures of Federal Awards and the Federal Financial Status reports.

Paragraph 4 of the policy states, “Agencies must load all their grants on the STARS Grant Control Table. This shall include funding percentages, revenue sources . . . and the applicable Catalog of Federal Domestic Assistance [CFDA].” Six of the CFDA numbers shown on the Schedule of Expenditures of Federal Awards (SEFA) for the fiscal year ended June 30, 2004, and 12 of the federal grant numbers had not been loaded into the STARS Grant Control Table.

Paragraph 5 states, “All grant awards must be recorded in the STARS Grant File.” The commission has not recorded any of its grant awards in the STARS Grant File.

Paragraph 7 states that “. . . drawdowns must be made utilizing the Daily Grant Drawdown Report of the STARS grant module. All reconciling items are to be clearly documented.” The commission does not use the Daily Grant Drawdown Report to support its drawdown amounts. Instead, it uses the invoices for reimbursement submitted by its subgrantees. As a result, the controls on the amounts and timing of drawdowns contained within the STARS grant module are not used.

Paragraph 9 states, “Agencies must utilize the STARS ‘Schedule of Grant Activity’ Report as the basis for preparing the Schedules of Expenditures of Federal Awards [SEFA].” The commission does not use this report as the basis. Instead, it uses information obtained from the invoices for reimbursement submitted by the Area Agencies and administrative cost allocations. The total on the SEFA is then reconciled to the STARS Spending/Receipt Plan YTD Status Report. Using this STARS report requires a more complicated reconciliation and thus increases the risk of errors. When the disbursement totals shown on the STARS “Schedule of Grant Activity” were compared with the totals shown on the FY04 SEFA, the STARS total was 14% less.

Paragraph 10 states, “Status Reports to the Federal government must be prepared utilizing STARS, including the grants module, as the basis with any reconciling items

documented.” The commission uses STARS, but not the grants module reports, for the administrative expenditures. Most of the expenditure information was obtained from the invoices for reimbursement submitted by the Area Agencies. There was no documented reconciliation to STARS. As a result, there is a greater risk that reporting errors could occur and not be detected in a timely manner.

When the commission does not follow F&A policies, it may not be maximizing the state’s resources and is increasing the probability that it might not report the financial activity of the federal programs accurately.

Recommendation

The Executive Director should direct the supervisor of fiscal and administrative services to implement the provisions of F&A Policy 20. If the Executive Director believes that the commission should be exempt from some or all of the requirements of this policy, she should instruct the supervisor of fiscal and administrative services to submit a written request to the Department of Finance and Administration’s Chief of Accounts requesting such exemption.

Management’s Comment

We concur.

The Commission’s Supervisor and Administrative Services met with the Department of Finance and Administration’s Director of STARS Development and Labor Distribution Coordinator, on July 26, 2005, to discuss the Commission implementation of Policy 20. They recommended the Commission plans to request a waiver from Policy 20. They further were advised that Grants Management would be looked at in the Enterprise Resources Planning (ERP) project as it is being developed. A letter requesting a waiver from Policy 20 is being submitted to Jan Sylvis, Chief of Accounts, Department of Finance and Administration.

SUPPLEMENTAL PAYROLL

Our objectives consisted of determining whether

- management had adequate controls in place to ensure that payroll rules and regulations related to supplemental payrolls were followed;
- payroll overpayments have been properly reported, the repayments have been made timely, and the amounts of overpayments were not excessive;
- supplemental pay was properly approved and in compliance with applicable laws and regulations; and
- payroll differentials were properly approved and in compliance with state laws and regulations.

We discussed with management the procedures used to ensure that payroll rules and regulations related to supplemental payrolls were followed and determined the adequacy of the procedures. We reviewed the correspondence on file at State Audit to determine if the commission had reported any overpayments during the audit period. There were no overpayments reported. We obtained a listing from SEIS of all payroll supplements related to payroll periods since July 1, 2001. Nothing came to our attention from a review of this listing that would indicate that the commission had made any overpayments. We tested all supplemental payrolls on the listing, excluding longevity payments, to determine if they had been properly approved and complied with the applicable rules and regulations. We asked management if any differentials had been paid since July 1, 2001. There were none; however, there were two payroll corrections. For both, we determined if the corrections were properly approved and complied with applicable rules and regulations.

As a result of our discussions and the subsequent testwork we concluded:

- management had adequate controls in place to ensure that payroll rules and regulations were followed,
- there were no payroll overpayments during the audit period,
- supplemental pay was properly approved and in compliance with applicable laws and regulations, and
- there were no payroll differentials.

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 commission's June 30, 2004; June 30, 2003; and June 30, 2002, 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 commission's evaluation of its internal accounting and administrative control was adequate;
- 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 have been implemented for material 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 commission's procedures. We also reviewed the June 30, 2004; June 30, 2003; and June 30, 2002, 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. The internal accounting and administrative control report did not identify any material weaknesses so no corrective action plan was required.

We concluded as a result of our discussions and review that

- the Financial Integrity Act responsibility letters and internal accounting and administrative control report were submitted on time except for the internal accounting and administrative control report that was due December 31, 2003, which was received at the Comptroller's office on January 21, 2004, 21 days late;
- documentation for the internal accounting and administrative control report was adequate; and
- 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*.

OBSERVATIONS AND COMMENTS

FRAUD CONSIDERATIONS

Statement on Auditing Standards No. 99 promulgated by the American Institute of Certified Public Accountants requires auditors to specifically assess the risk of material misstatement of an audited entity's financial statements due to fraud. The standard also restates the obvious premise that management, and not the auditors, is primarily responsible for preventing and detecting fraud in its own entity. Management's responsibility is fulfilled in part when it takes appropriate steps to assess the risk of fraud within the entity and to implement adequate internal controls to address the results of those risk assessments.

During our audit, we discussed these responsibilities with management and how management might approach meeting them. We also increased the breadth and depth of our inquiries of management and others in the entity as we deemed appropriate. We obtained formal assurances from top management that management had reviewed the entity's policies and procedures to ensure that they are properly designed to prevent and detect fraud and that management had made changes to the policies and procedures where appropriate. Top

management further assured us that all staff had been advised to promptly alert management of all allegations of fraud, suspected fraud, or detected fraud and to be totally candid in all communications with the auditors. All levels of management assured us there were no known instances or allegations of fraud that were not disclosed to us.

AUDIT COMMITTEE RECOMMENDED

As a result of the fraud-related business failures of companies such as Enron and WorldCom in recent years, Congress and the accounting profession have taken aggressive measures to try to detect and prevent future failures related to fraud. These measures have included the signing of the *Sarbanes-Oxley Act of 2002* by the President of the United States and the issuance of Statement on Auditing Standards No. 99 by the American Institute of Certified Public Accountants. This new fraud auditing standard has not only changed the way auditors perform audits but has also provided guidance to management and boards of directors on creating antifraud programs and controls. This guidance has included the need for an independent audit committee.

As a result of these developments, we are recommending that agencies with boards establish audit committees. The specific activities of any audit committee will depend on, among other things, the mission, nature, structure, and size of each agency. In establishing the audit committee and creating its charter, each board should examine its commission's particular circumstances. Anti-fraud literature notes that there are two categories of fraud: fraudulent financial reporting and misappropriation of assets. The audit committee should consider the risks of fraud in this commission in general as well as the history of this particular commission with regard to prior audit findings, previously disclosed weaknesses in internal control, and compliance issues. The audit committee should consider both the risk of fraudulent financial reporting and the risk of fraud due to misappropriation or abuse of commission assets. Also, the board and the audit committee should keep in mind that agencies receiving public funding should have a lower threshold of materiality than private sector entities with regard to fraud risks.

Boards should exercise professional judgment in establishing the duties, responsibilities, and authority of their audit committee. The factors noted below are not intended to be an exhaustive listing of those matters to be considered. The committee should not limit its scope to reacting to a preconceived set of issues and actions but rather should be proactive in its oversight of the commission as it concentrates on the internal control and audit-related activities of the entity. In fact, this individualized approach is one of the main benefits derived from an audit committee.

At a minimum, audit committees should:

1. Develop a written charter that addresses the audit committee's purpose and mission, which should be, at a minimum, to assist the board in its oversight of the commission.
2. Formally reiterate, on a regular basis, to the board, commission management, and staff their responsibilities for preventing, detecting, and reporting fraud, waste, and abuse.

3. Serve as a facilitator of any audits or investigations of the commission, including advising auditors and investigators of any information they may receive or otherwise note regarding risks of fraud or weaknesses in the commission's internal controls; reviewing with the auditors any findings or other matters noted by the auditors during audit engagements; working with the commission management and staff to ensure implementation of audit recommendations; and assisting in the resolution of any problems the auditors may have with cooperation from commission management or staff.
4. Develop a formal process for assessing the risk of fraud at the commission, including documentation of the results of the assessments and assuring that internal controls are in place to adequately mitigate those risks.
5. Develop and communicate to staff of the commission their responsibilities to report allegations of fraud, waste, or abuse at the agency to the committee and the Comptroller of the Treasury's office as well as a process for immediately reporting such information.
6. Immediately inform the Comptroller's office when fraud is detected.
7. Develop and communicate to the board, commission management, and staff a written code of conduct reminding those individuals of the public nature of the commission and the need for all to maintain the highest level of integrity with regard to the financial operations and any related financial reporting responsibilities of the agency; to avoid preparing or issuing fraudulent or misleading financial reports or other information; to protect agency assets from fraud, waste, and abuse; to comply with all relevant laws, rules, policies, and procedures; and to avoid engaging in activities which would otherwise bring dishonor to the commission.

The charter of the audit committee should include, at a minimum, the following provisions:

1. The audit committee should be a standing committee of the board.
2. The audit committee should be composed of at least three members. The chair of the audit committee should preferably have some accounting or financial management background. Each member of the audit committee should have an adequate background and education to allow a reasonable understanding of the information presented in the financial reports of the commission and the comments of auditors with regard to internal control and compliance findings and other issues.
3. The members of the audit committee must be independent from any appearances of other interests that are in conflict with their duties as members of the audit committee.
4. An express recognition that the board, the audit committee, and the management and staff of the commission are responsible for taking all reasonable steps to prevent, detect, and report fraud, waste, and abuse.
5. The audit committee should meet regularly throughout the year. The audit committee can meet by telephone, if that is permissible for other committees. However, the audit committee is strongly urged to meet at least once a year in person. Members of

the audit committee may be members of other standing committees of the board, but the audit committee meetings should be separate from the meetings of other committees of the board.

6. The audit committee should record minutes of its meetings.

The Division of State Audit will be available to discuss with the board any questions it might have about the creation of its particular audit committee. There are also other audit committees which have already been established at other state agencies that the board may wish to contact for advice and further information.

APPENDIX

ALLOTMENT CODE

The Tennessee Commission on Aging and Disability uses allotment code 316.02.