AUDIT REPORT

Department of the Treasury

For the Year Ended
June 30, 2005

STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
Department of Audit
Division of State Audit

Arthur A. Hayes, Jr., CPA, JD, CFE
Director

Edward Burr, CPA
Assistant Director

Teresa L. Hensley, CPA
Audit Manager

Blayne Clements
Teresa L. Kennedy, CPA
In-Charge Auditors

Lana Bland, CFE
David Cook
Mary McCalip, CFE
Andy Summar, CPA, CFE
Staff Auditors

Gerry C. Boaz, CPA
Technical Analyst

Amy Brack
Editor

Comptroller of the Treasury, Division of State Audit
1500 James K. Polk Building, Nashville, TN 37243-0264
(615) 401-7897

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STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
State Capitol
Nashville, Tennessee 37243-0260
(615) 741-2501

John G. Morgan
Comptroller

March 23, 2006

Members of the General Assembly
and
The Honorable Dale Sims, Treasurer
State Capitol
Nashville, Tennessee 37243

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Department of the Treasury for the year ended June 30, 2005.

Consideration of internal control over financial reporting and tests of compliance disclosed a deficiency, which is detailed in the Results of the Audit section of this report. The department's management has responded to the audit finding; the response is included following the finding. The Division of State Audit will follow up the audit to examine the application of the procedures instituted because of the audit finding.

Sincerely,

John G. Morgan
Comptroller of the Treasury

JGM/fd
05/094

State of Tennessee

Audit Highlights

Comptroller of the Treasury — Division of State Audit

Financial and Compliance Audit

Department of the Treasury

For the Year Ended June 30, 2005

AUDIT OBJECTIVES

The objectives of the audit were to consider the Department of the Treasury's internal control over financial reporting to determine auditing procedures for the purpose of expressing an opinion on the financial statements of the Baccalaureate Education System Trust-Educational Services Plan, the Chairs of Excellence Fund, the Criminal Injuries Compensation Fund, the Flexible Benefits Plan, the Risk Management Fund, the Small and Minority-Owned Business Assistance Program Fund, and the State Pooled Investment Fund; to determine compliance with certain provisions of laws, regulations, contracts, and grant agreements; and to recommend appropriate actions to correct any deficiencies.

INTERNAL CONTROL FINDING

Controls Over Certain Local Government Investment Pool Transactions Are Inadequate and Could Permit Unauthorized Withdrawals

A lack of segregation of duties exists in the performance of certain Local Government Investment Pool (LGIP) transactions that creates an opportunity for fraud. An employee with the capability to both initiate and release the transaction could use an LS type of transaction to divert LGIP participant funds to an unauthorized bank account (page 13).

Audit Report
Department of the Treasury
For the Year Ended June 30, 2005

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Department of the Treasury
For the Year Ended June 30, 2005

INTRODUCTION

POST-AUDIT AUTHORITY

This is a report on the financial and compliance audit of the Department of the Treasury. The audit was conducted pursuant to Section 4-3-304, *Tennessee Code Annotated*, which authorizes 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 State Treasurer, a constitutional officer, is elected by a joint session of the General Assembly for a two-year term. Although no duties are prescribed by the constitution, the functions and duties of the office are assigned through various statutes. These functions and duties include maintaining accountability for and management of public funds and administering the Tennessee Consolidated Retirement System, the State Pooled Investment Fund (including the Local Government Investment Pool), the Uniform Disposition of Unclaimed Property Act, the Criminal Injuries Compensation Fund, the Chairs of Excellence Fund, the Baccalaureate Education System Trust, the Small and Minority-Owned Business Assistance Program, and the state's Deferred Compensation and Flexible Benefits plans. The Treasurer also administers the settlement of claims against the state through the Tennessee Claims Commission and the Division of Claims Administration.

The Treasurer is required by statute to be a member of many boards and commissions, including the following:

Board of Equalization
Board of Trustees of the Tennessee Consolidated Retirement System
Funding Board
Public Records Commission
State Building Commission
State Insurance Committee

State School Bond Authority
Tennessee Competitive Export Corporation
Tennessee Housing Development Agency
Tennessee Local Development Authority
Tennessee Student Assistance Corporation

ORGANIZATION

The department is divided into 11 major sections: Staff Services, Investments, Baccalaureate Education System Trust (BEST), Information Systems, Records Management, State Trust and Lock Box, Tennessee Consolidated Retirement System (TCRS), Accounting, Unclaimed Property, Claims Administration, and Risk Management. The TCRS is audited and reported on separately.

The **Staff Services** section includes personnel administration, budgeting and fiscal control, administrative services, research and development of special projects, internal audit, and legal services.

The **Investments** section invests the pension fund to maximize the return on investments and to protect the retirement system's assets. This section also invests the state's available cash in certificates of deposit in state depositories, prime commercial paper, prime bankers' acceptances, certain repurchase agreements, various U.S. Treasury and agency obligations, and certain obligations of the State of Tennessee.

The **BEST** section is responsible for the operation of the state's prepaid college tuition plan (Educational Services Plan) and college savings plan (Educational Savings Plan).

The **Information Systems** section provides the department with data processing services. The **Records Management** section provides physical facilities management, forms control and copying, and safekeeping. **State Trust and Lock Box** is responsible for remittance receiving and the operation of the Federal Reserve wire transfer facility used to send, receive, and transfer funds for the State of Tennessee.

The **Accounting** section is responsible for maintaining detailed accounting records for various programs administered by the department. This includes maintaining general ledger accounting and reporting for the Tennessee Consolidated Retirement System, the Chairs of Excellence Program, the Local Government Investment Pool, the Cash Management Investment Program, the Risk Management Fund, the Criminal Injuries Compensation Fund, the Flexible Benefits Plan, the Baccalaureate Education System Trust, and the Small and Minority-Owned Business Assistance Program. The section is also responsible for reconciling approximately 80 open bank accounts and maintaining the state's warrant reconciliation system (Account Reconciliation Package, or ARP).

The **Unclaimed Property** section takes custody of abandoned property (bank accounts, insurance policies, etc.) and attempts to locate the rightful owners or heirs. The Division of **Claims Administration** administers the Workers' Compensation program for state employees and the Criminal Injuries Compensation Fund. The division reviews and determines eligibility for payment from the Criminal Injuries Compensation Fund. Payments are made as funds become available.

The **Risk Management** section administers a variety of insurance programs for the state. These programs provide protection to the state against property damage, boiler explosion, and employee dishonesty.

The department is currently developing an assistance program for small and minority-owned businesses, which may include loans and loan guarantees, technical assistance, and program services.

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

AUDIT SCOPE

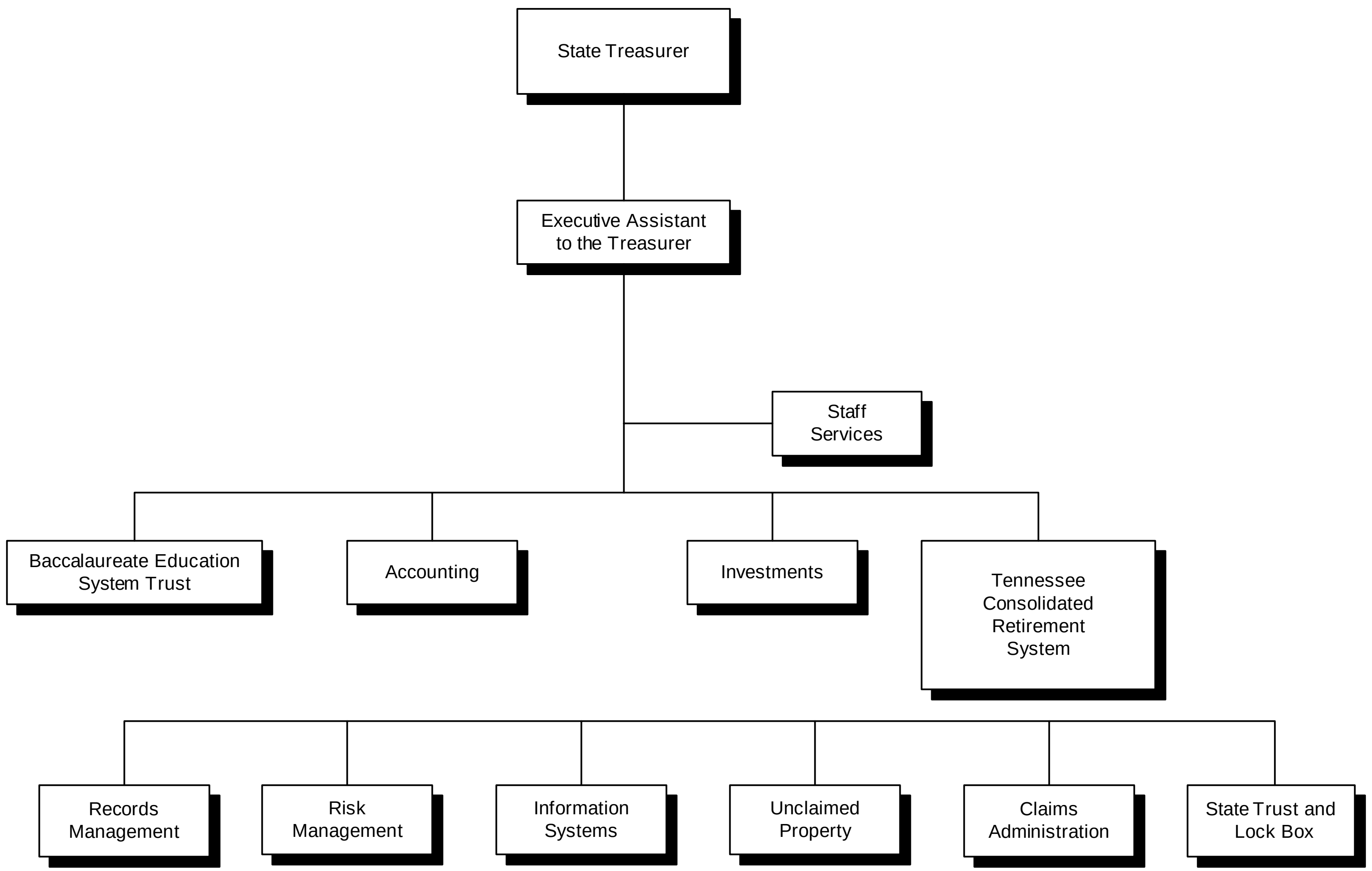
The audit was limited to the period July 1, 2004, through June 30, 2005, and was conducted in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

The operations of the Department of the Treasury are accounted for in the general fund of the State of Tennessee. The department administers the Tennessee Consolidated Retirement System, pension trust funds; the Criminal Injuries Compensation Fund and the Small and Minority-Owned Business Assistance Program Fund, special revenue funds; the Risk Management Fund, an internal service fund; the Chairs of Excellence Fund, a permanent fund; the Baccalaureate Education System Trust-Educational Services Plan, a private-purpose trust fund; the Flexible Benefits Plan, an employee benefit trust fund; and the State Pooled Investment Fund, an external investment pool (which includes the Local Government Investment Pool).

This audit included all of the above funds except for the Tennessee Consolidated Retirement System, which is reported on in a separate audit report. The following allotment codes within the State of Tennessee Accounting and Reporting System were covered by this audit:

State Treasurer's Office	309.01
Certified Public Administrators	309.02
Small and Minority-Owned Business Assistance Program	309.05
Criminal Injuries Compensation	313.03

Department of the Treasury
Organization Chart



Risk Management Fund	313.10
Unclaimed Property	313.20

OBJECTIVES OF THE AUDIT

The objectives of the audit were

1. to consider the Department of the Treasury's internal control over financial reporting to determine auditing procedures for the purpose of expressing an opinion on the financial statements of the Baccalaureate Education System Trust-Educational Services Plan, the Chairs of Excellence Fund, the Criminal Injuries Compensation Fund, the Flexible Benefits Plan, the Risk Management Fund, the Small and Minority-Owned Business Assistance Program Fund, and the State Pooled Investment Fund;

2. to determine compliance with certain provisions of laws, regulations, contracts, and grant agreements; and

3. to recommend appropriate actions to correct any deficiencies.

Although this audit was not intended to serve as an organization-wide audit as described in the Single Audit Act, as amended by the Single Audit Act Amendments of 1996, and Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations,* it included tests of compliance with applicable federal laws and regulations and consideration of internal control used in administering federal financial assistance programs. This audit is a segment of the organization-wide audit of the State of Tennessee, which is conducted in accordance with the Single Audit Act.

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 Department of the Treasury filed its report with the Department of Audit on June 13, 2005. A follow-up of the prior audit finding was conducted as part of the current audit.

The current audit disclosed that the department has corrected the previous audit finding concerning inadequate user controls over claims.

OBSERVATIONS AND COMMENTS

MANAGEMENT'S RESPONSIBILITY FOR RISK ASSESSMENT

Auditors and management are required to assess the risk of fraud in the operations of the entity. The risk assessment is based on a critical review of operations considering what frauds could be perpetrated in the absence of adequate controls. The auditors' risk assessment is limited to the period during which the audit is conducted and is limited to the transactions that the auditors are able to test during that period. The risk assessment by management is the primary method by which the entity is protected from fraud, waste, and abuse. Since new programs may be established at any time by management or older programs may be discontinued, that assessment is ongoing as part of the daily operations of the entity.

Risks of fraud, waste, and abuse are mitigated by effective internal controls. It is management's responsibility to design, implement, and monitor effective controls in the entity. Although internal and external auditors may include testing of controls as part of their audit procedures, these procedures are not a substitute for the ongoing monitoring required of management. After all, the auditor testing is limited and is usually targeted to test the effectiveness of particular controls. Even if controls appear to be operating effectively during the time of the auditor testing, they may be rendered ineffective the next day by management override or by other circumventions that, if left up to the auditor to detect, will not be noted until the next audit engagement and then only if the auditor tests the same transactions and controls. Furthermore, since staff may be seeking to avoid auditor criticisms, they may comply with the controls during the period that the auditors are on site and revert to ignoring or disregarding the control after the auditors have left the field.

The risk assessments and the actions of management in designing, implementing, and monitoring the controls should be adequately documented to provide an audit trail both for auditors and for management, in the event that there is a change in management or staff, and to maintain a record of areas that are particularly problematic. The assessment and the controls should be reviewed and approved by the head of the entity.

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 COMMITTEES

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.

In the previous audit report, we recommended that the Department of the Treasury establish audit committees for the various boards governing their funds. As of the end of our audit, the board of the Chairs of Excellence Trust has elected an audit committee and adopted a charter, but the charter has not yet been approved by the Comptroller of the Treasury as required by the State of Tennessee Audit Committee Act of 2005. The board of the Baccalaureate Education System Trust-Educational Services Plan has not elected an audit committee or adopted a charter as of the end of our audit. In recognition of the benefits of audit committees for government, the Tennessee General Assembly has enacted legislation known as the "State of Tennessee Audit Committee Act of 2005." This legislation requires the creation of audit committees for those entities that have governing boards, councils, commissions, or equivalent bodies that can hire and terminate employees and/or are responsible for the preparation of financial statements. Applicable entities are required to develop an audit committee charter and appoint the audit committee in accordance with the legislation. 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 agency'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 its agency in general as well as the history of its particular agency 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 agency 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 agency 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 agency.
2. Formally reiterate, on a regular basis, to the board, agency 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 agency, including advising auditors and investigators of any information they may receive or otherwise note regarding risks of fraud or weaknesses in the agency's internal controls; reviewing with the auditors any findings or other matters noted by the auditors during audit engagements; working with the agency management and staff to ensure implementation of audit recommendations; and assisting in the resolution of any problems the auditors may have with cooperation from agency management or staff.
4. Develop a formal process for assessing the risk of fraud at the agency, 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 agency 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, agency management, and staff a written code of conduct reminding those individuals of the public nature of the agency 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 agency.

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 agency 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 agency 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 boards any questions they might have about the creation of their particular audit committees. There are also other audit committees which have already been established at other state agencies that the boards may wish to contact for advice and further information.

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 the Treasury filed its compliance report and implementation plan on June 30, 2005.

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.

RESULTS OF THE AUDIT

AUDIT CONCLUSIONS

Internal Control

As part of the audit of the financial statements of the Baccalaureate Education System Trust-Educational Services Plan, the Chairs of Excellence Fund, the Criminal Injuries Compensation Fund, the Flexible Benefits Plan, the Risk Management Fund, the Small and Minority-Owned Business Assistance Program Fund, and the State Pooled Investment Fund for the year ended June 30, 2005, we considered internal control over financial reporting to determine auditing procedures for the purpose of expressing an opinion on the financial statements, as required by auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. A reportable condition, along with the recommendation and management's response, is detailed in the Finding and Recommendation section of this report. Consideration of internal control over financial reporting disclosed no material weaknesses.

Compliance and Other Matters

The results of our audit tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
DEPARTMENT OF AUDIT
DIVISION OF STATE AUDIT
SUITE 1500
JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-0264
PHONE (615) 401-7897
FAX (615) 532-2765

Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards*

December 15, 2005

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

Dear Mr. Morgan:

We have audited the financial statements of the Baccalaureate Education System Trust-Educational Services Plan, the Chairs of Excellence Fund, the Criminal Injuries Compensation Fund, the Flexible Benefits Plan, the Risk Management Fund, the Small and Minority-Owned Business Assistance Program Fund, and the State Pooled Investment Fund as of and for the year ended June 30, 2005, and have issued our report thereon dated December 15, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. The Department of the Treasury and the funds it administers are part of the primary government of the State of Tennessee.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the department's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted a matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the department's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

The following reportable condition was noted: Controls over certain Local Government Investment Pool transactions are inadequate and could permit unauthorized withdrawals. This condition is described in the Finding and Recommendation section of this report.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we do not believe that the reportable condition described above is a material weakness.

We also noted certain matters involving the internal control over financial reporting, which we have reported to the department's management in a separate letter.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of the department's compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We did, however, note certain less significant instances of noncompliance which we have reported to the department's management in a separate letter.

This report is intended solely for the information and use of the General Assembly of the State of Tennessee and management and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record.

Sincerely,

Arthur A. Hayes, Jr., CPA
Director

AAH/fd

FINDING AND RECOMMENDATION

<u>Controls over certain Local Government Investment Pool transactions are inadequate and could permit unauthorized withdrawals</u>

Finding

Tennessee municipalities, counties, school districts, utility districts, community service agencies, local government units, and political subdivisions can deposit monies with the Treasurer to be invested in the state cash management investment pool. This is referred to as the Local Government Investment Pool (LGIP). Treasury employees in the cash management division have access to account information and can make deposits, withdrawals, and transfers of funds from LGIP participant accounts. A lack of segregation of duties exists in the performance of certain LGIP transactions that creates an opportunity for fraud.

Five employees have the capability to both initiate and release LGIP transactions. When a withdrawal is placed in release status, wire room personnel wire the funds to the account designated by the initiator of the transaction. Under normal circumstances, a compensating control exists whereby the bank account information must be entered by an individual independent of cash management and wire room duties, and, when doing so, various steps are taken to ensure the validity of the account. However, on occasions when the LGIP wire must be sent through the State Trust rather than through the contracted agent bank, these five employees are also responsible for entering the destination bank account information. These are referred to as "LS" transactions. An employee with the capability to both initiate and release the transaction could use an LS type of transaction to divert LGIP participant funds to an unauthorized bank account. Therefore, there is the potential for a material loss since the amount of a withdrawal is only limited by the balance in the account, and one withdrawal transaction could draw funds from multiple accounts. For perspective, at June 30, 2005, total LGIP funds amounted to $1,633,649,355. The largest account comprised $105,980,563 of that total. Management does not require any reviews or approvals for the performance of LS transactions. Therefore, possible detection of a withdrawal to an unauthorized bank account would not occur until participants enrolled in the web-based system reviewed their account activity on-line or, for those not enrolled, possible detection would not occur until they received their LGIP statement at the end of the month. Those controls assume the participants actively review and reconcile their account activity.

There were a total of 33 LS transactions that occurred during the year ended June 30, 2005. All of these transactions were tested for propriety of the destination account. We noted no improprieties as a result of that work.

Recommendation

As is done with all other LGIP transactions, the Director of Cash Management should require an individual independent of cash management and wire room duties to input the destination account information for LS transactions. Personnel who have the ability to both initiate and release an LGIP transaction should not have the ability to enter a destination account.

Management should ensure that risks such as these noted in this finding are adequately identified and assessed in management's documented risk assessment activities. Management should identify specific staff to be responsible for the design and implementation of internal controls to adequately mitigate those risks and to prevent and detect exceptions timely. Management should also identify staff to be responsible for ongoing monitoring for compliance with all requirements and taking prompt action should exceptions occur. All controls and control activities, including monitoring, should be adequately documented.

Management's Comment

Management concurs. When this was brought to management's attention during the course of the audit, management immediately made the appropriate change to the software program to eliminate this potential weakness. The software program was changed to process LS transactions in the same manner as other LGIP transactions. Cash Management employees can no longer input the destination account information. In addition, staff independent of cash management and the wire room is responsible for inputting destination account information into the system. Of the 4,069 LGIP withdrawal transactions processed during the year ended June 30, 2005, only 33 LS transactions were processed.

Management of the department has historically acknowledged its responsibility for assessment of risks, identification of staff responsible for the design and implementation of internal controls to mitigate those risks and to prevent and detect exceptions timely, and identification of staff responsible for ongoing monitoring for compliance with all requirements and taking prompt action should exceptions occur. Management believes its actions, both past and present, reflect a commitment to a proactive approach in these areas. We believe the department's record of ongoing consideration of internal controls, work performed to fulfill the requirements of the Financial Integrity Act, and actions taken in response to findings of both internal and external audits is evidence of management's commitment to risk assessment, control, and monitoring. Management continually strives to improve its process for assessing areas of risk and for strengthening internal controls to mitigate those risks.