

# AUDIT REPORT

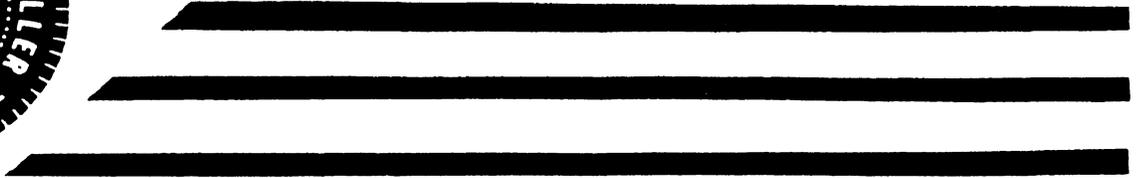
Department of Agriculture

November 2007



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

State Capitol  
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John G. Morgan  
Comptroller

November 29, 2007

The Honorable Phil Bredesen, Governor  
and

Members of the General Assembly  
State Capitol  
Nashville, Tennessee 37243

and

The Honorable Ken Givens, Commissioner  
Department of Agriculture  
Ellington Agricultural Center  
Nashville, Tennessee 37204

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Department of Agriculture for the period March 1, 2004, through May 31, 2007.

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/to  
07/059



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**COMPTROLLER OF THE TREASURY**  
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June 5, 2007

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

Dear Mr. Morgan:

We have conducted a financial and compliance audit of selected programs and activities of the Department of Agriculture for the period March 1, 2004, through May 31, 2007.

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

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

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

Sincerely,

Arthur A. Hayes, Jr., CPA  
Director

AAH/to

State of Tennessee

# Audit Highlights

Comptroller of the Treasury

Division of State Audit

Financial and Compliance Audit  
**Department of Agriculture**  
November 2007

## AUDIT SCOPE

We have audited the Department of Agriculture for the period March 1, 2004, through May 31, 2007. 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 cash receipts, payment cards, equipment, Department of Finance and Administration Policy 16–*Employee Housing and Meals*, expenditures, 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

### **Management Has Not Adequately Assessed and Mitigated the Risks Associated With Inadequate Controls Over Cash Receipting\***

Neither the department's fiscal staff nor its division staff perform reconciliations between licenses, certifications, and registrations issued and revenue collected and deposited (page 6).

### **Staff Did Not Always Follow the State's Policies and Procedures for Payment Cards, Which Increases the Risk of Fraudulent Activity**

The agency coordinator did not always maintain specific cardholder documentation for new cardholders. Also, four individuals

had active accounts even though three were not current employees and one was not issued the payment card. Two cardholders indicated that they had loaned their assigned payment card to another person and that not all purchases were made by the authorized cardholders (page 8).

### **The Property Officer Did Not Complete the Equipment Inventory Process**

The property officer did not complete the annual inventory by June 30, 2006, and did not request the equipment exception report from the Department of General Services until February 2007 (page 12).

\* This finding is repeated from prior audits.

# Financial and Compliance Audit Department of Agriculture

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# Financial and Compliance Audit Department of Agriculture

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## INTRODUCTION

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### POST-AUDIT AUTHORITY

This is the report on the financial and compliance audit of the Department of Agriculture. 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

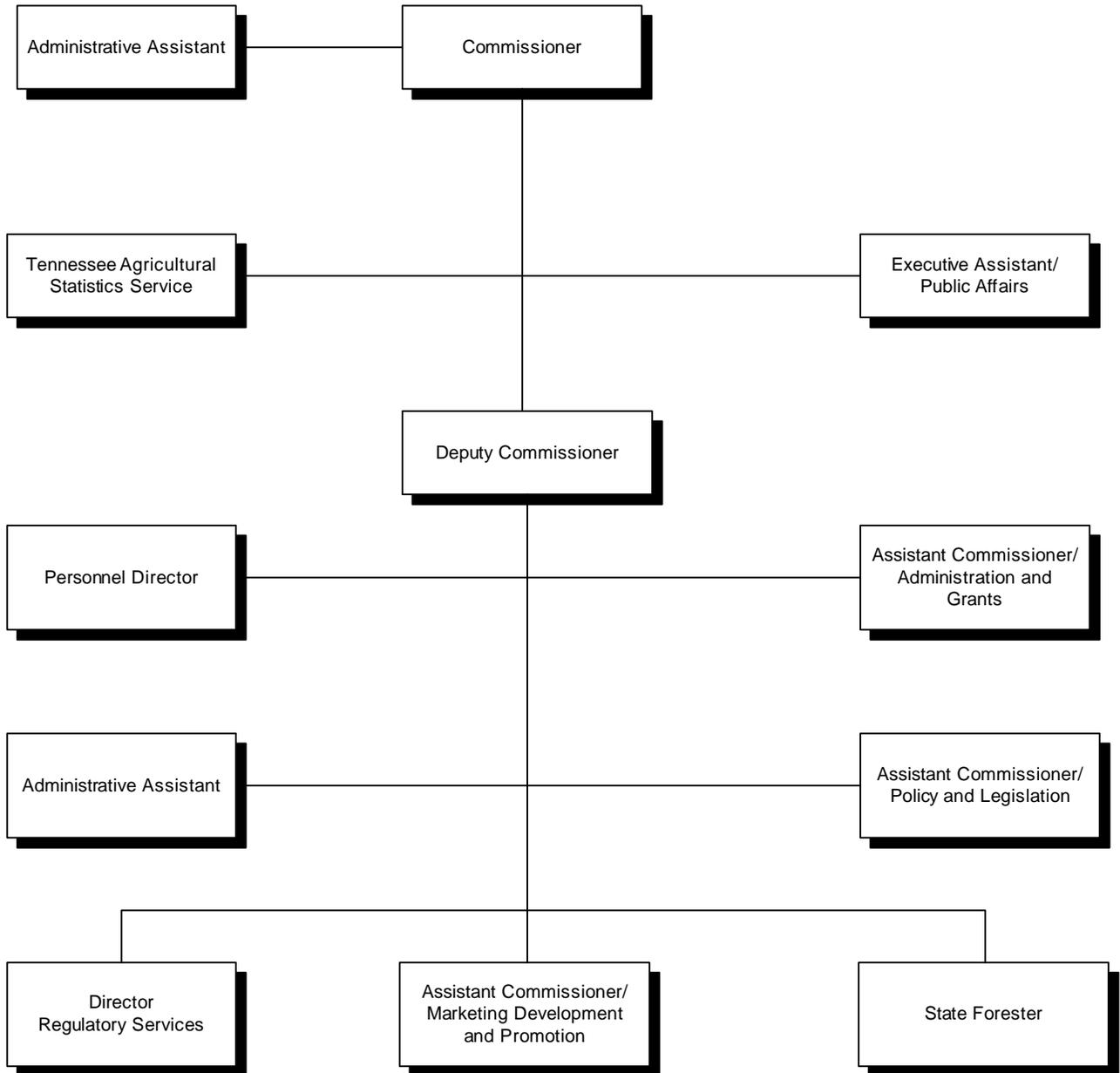
The Department of Agriculture’s mission is to improve the livelihood of farmers, forestland owners, consumers, and the state’s agri-industries through sustaining our natural resources, enforcing clear and effective regulations, and maximizing economic opportunities. The department has the following powers and responsibilities:

1. to encourage and promote the interests of agriculture, including forestry, horticulture, the livestock industry, the dairy industry, poultry raising, beekeeping, wool production, and other allied industries;
2. to collect, publish, and distribute statistics relating to crop production and marketing and to the production and marketing of beef, pork, poultry, and other agricultural products;
3. to inquire into the cause of contagious, infectious, and communicable disease among domestic animals and to seek prevention and cure of disease;
4. to assist, encourage, and promote the organization of farmers’ institutes and agricultural societies and the holding of fairs, stock shows, or other exhibits of agricultural products;
5. to cooperate with the University of Tennessee Agricultural Extension Service and the United States Department of Agriculture;

6. to inspect any place where fruits are grown or stored, to inspect any plant life for pests or diseases, and to strive toward eradication of these pests or diseases;
7. to assist the Soil Conservation Districts and the State Soil Conservation Committee in discharging duties described in the Soil Conservation District Act of 1939;
8. to support the proper management and development of forest resources in Tennessee for public and private benefit through programs of forest protection, landowner assistance, and reforestation;
9. to inspect and regulate retail food stores, food service establishments, food manufacturers, food warehouses, food distributors, and dairy farms and plants;
10. to perform custom slaughterhouse inspections, hazardous substance inspections, and egg shell inspections;
11. to ensure compliance with regulations for nutritional labeling, hazardous substance labeling, consumer product safety, bottled water, and the enforcement of state tobacco laws regarding sales to minors;
12. to regulate motor fuels sold within the state for quality and correct octane levels;
13. to license certified public weighers and weighmasters and to inspect scales used across the state;
14. to register pesticide products and regulate their sale and use for both agricultural and structural purposes and to regulate pest control businesses and dealers in the storage, handling, and application of pesticides;
15. to plan and maintain vigilance for and ensure appropriate responses to potential and actual agroterrorism and to coordinate activities with the state Office of Homeland Security and other state and federal agencies;
16. to support the activities and policies of the Tennessee Tobacco Farmers Certifying Board in administering the allocation of funds from the National Tobacco Growers Settlement Trust (Phase II); and
17. to increase farm income in the state through the domestic and international marketing and promotion of Tennessee grown and processed agricultural products and services and through the recruitment and development of agri-industries that create jobs and markets for farm products.

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

# Department of Agriculture Organization Chart



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## AUDIT SCOPE

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We have audited the Department of Agriculture for the period March 1, 2004, through May 31, 2007. 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 cash receipts, payment cards, equipment, Department of Finance and Administration Policy 16–*Employee Housing and Meals*, expenditures, 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.

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## PRIOR AUDIT FINDINGS

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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 Agriculture filed its report with the Department of Audit on December 2, 2004. A follow-up of all prior audit findings was conducted as part of the current audit.

### RESOLVED AUDIT FINDING

The current audit disclosed that the Department of Agriculture has corrected the previous audit finding concerning the department not complying with state policy on providing housing to state employees.

### REPEATED AUDIT FINDING

The prior audit report also contained a finding concerning controls over cash receipting and licensing needing improvement. This finding has not been completely resolved and is repeated in the applicable section of this report.

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## OBJECTIVES, METHODOLOGIES, AND CONCLUSIONS

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### CASH RECEIPTS

Our objectives for reviewing cash receipts were to follow up a prior audit finding and determine whether

- the procedures for assessing and collecting fees were adequate;
- cash receipts were properly accounted for and deposited timely;
- reconciliations between licenses, certificates, or registrations issued and revenue received and deposited were performed; and
- proper receipting procedures, including mail logs, written receipts, and proper segregation of duties, were in place.

We interviewed key department personnel in the Animal Health, Pesticides, Plant Certifications, Food and Dairy, Nursery, and Administration divisions to gain an understanding of the department's controls and procedures over cash receipts and to determine whether proper receipting procedures, including mail logs, written receipts, and proper segregation of duties, were in place. We also tested a nonstatistical sample of cash receipts for the department to determine if the proper fees were assessed and collected and if the receipts were properly accounted for and deposited timely. We interviewed key department personnel to determine whether reconciliations between licenses, certificates, or registrations issued and revenue received and deposited were performed.

Based on interviews and reviews of supporting documentation, we determined that proper receipting procedures, including mail logs, written receipts, and proper segregation of duties, were in place. Based on our testwork, we determined that the procedures for assessing and collecting fees were adequate, and cash receipts were properly accounted for and deposited timely. However, the department did not perform proper reconciliations between licenses, certificates, or registrations issued and the revenue received and deposited. This weakness is discussed in finding 1.

**1. Management has not adequately assessed and mitigated the risks associated with inadequate controls over cash receipting, and as a result, the department cannot ensure that all funds have been properly collected and deposited**

**Finding**

The Department of Agriculture collects fees in its various divisions for issuing licenses, certifications, and registrations and for fines, products, and services. The department receives the majority of these fees in the mail and to a lesser extent from walk-in clients. As noted in the two prior audits, the department's controls over the cash receipting procedures for these fee collections need improvement. Management concurred with the prior findings and stated that they planned to consolidate revenue collection and perform independent reconciliations of licenses, certifications, and registrations to cash receipts and deposits. In response to the prior finding, management and staff implemented significant changes in the cash receipting process. These improvements included:

- Mailroom employees and Plant Certification administrative staff prepare cash receipt listings when cash is received in the mail.
- Animal Health Division staff prepare cash receipt listings before the licenses are issued.
- Staff prepare reconciliations between the receipts issued by inspectors in the field and the deposits made.
- In the Animal Health Division, management has segregated the duties of the employee responsible for preparing licenses. This employee no longer has access to the checks before they are deposited.

However, management has not yet established procedures to reconcile all licenses, certifications, and registrations issued to revenue collected and deposited.

Based on observations and discussions with the fiscal director and the division administrators, we determined that neither the department's fiscal staff nor its division staff perform reconciliations between licenses, certifications, and registrations issued and revenue collected and deposited. Because the department has not been reconciling licenses, certifications, and registrations issued with revenue collected and deposited, it cannot be certain all funds have been properly collected and deposited. In addition, because the department has not effectively mitigated its risk by performing reconciliations, the risk of fraud by department staff is increased. However, we did not find any evidence of fraud.

**Recommendation**

The Commissioner should assign specific responsibility to staff, independent of the licensing and receipting functions, for periodically reconciling licenses, certifications, and registrations issued with revenue received and deposited. The individuals who are given the

responsibility for performing reconciliations should be given clear, written guidance on how to perform the reconciliations and how their efforts contribute to the control environment. The Commissioner should also assign specific responsibility to staff for ongoing monitoring for compliance. Those individuals should also be given clear, written guidance, including the need to take prompt corrective actions should deficiencies occur.

In addition, the Commissioner should ensure that other risks of improper accountability, noncompliance, fraud, waste, or abuse are adequately identified and assessed in management's documented risk assessment. Management should implement effective controls to ensure compliance with applicable requirements and should assign staff to be responsible for ongoing monitoring of the risks and mitigating controls and take action if deficiencies occur.

### **Management's Comment**

We concur. The Department of Agriculture, specifically the Regulatory Services division, issues thousands of permits, licenses, and registrations each year. Due to the high number of licenses, permits, and registrations issued each year, the Department of Agriculture is currently working to implement a systemic reconciliation process. The systemic reconciliation process will track issued permits, licenses, and registrations to the revenue received via a control number. Additionally, the reconciliation will include an issuance report which correlates licenses, permits, and registrations issued to revenue received. An exception report will identify any licenses, permits, or registrations issued without the receipt of revenue. Both the issuance report and exception report will be distributed to management to ensure follow-up action is taken.

The Department of Agriculture's Internal Auditor will monitor the progress of the project and ensure proper controls are in place. Key personnel conducted an initial meeting on September 26, 2007. Future meetings will be held as needed to ensure this finding is addressed.

Additionally, the Department of Agriculture's risk assessment addresses the risks of noncompliance, fraud, waste, and abuse. Management was also asked to identify the controls in place to mitigate the risks. Testing of the identified controls is in progress. Any process or procedural changes deemed necessary will be implemented.

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### **PAYMENT CARDS**

Our objectives in reviewing controls and procedures over the use of payment cards were to determine whether

- cardholders were current department employees and were properly approved;
- payment card purchases were adequately supported and recorded on the transaction logs;

- payment card purchases appeared reasonable and necessary for the conduct of state business and exceeded the single-purchase dollar limit;
- payment card purchases complied with the Department of General Services' *Agency Purchasing Procedures Manual*;
- payment card transaction logs were properly approved; and
- department staff reconciled the transaction logs to the statements.

We reviewed the applicable laws and regulations, interviewed key personnel, and reviewed supporting documentation to gain an understanding of the controls and procedures over payment cards. We tested a nonstatistical sample of new cardholders from March 1, 2004, through February 14, 2007, to determine if the cardholders were current department employees and if they had received the required approvals to be valid cardholders. We tested several nonstatistical samples of payment card transactions made during the period March 1, 2004, to January 15, 2007, for adequate documentation, reconciliation to the transaction logs, and compliance with the Department of General Services' *Agency Purchasing Procedures Manual*. These samples were selected from all payment card transactions, transactions from suspicious vendors, transactions made on a weekend or a state holiday, and transactions with unusual merchant category codes. We also tested for purchases which exceeded the single-purchase dollar limit and to determine if the purchases appeared reasonable and necessary for the conduct of state business. We reviewed a sample of transaction logs for proper approvals and reconciliation to the statements.

Based on testwork performed related to new cardholders, we determined that not all cardholders were current department employees and that one employee had an active account but was never issued a card; that applications and cardholder and approver agreements were not always properly approved; and that cardholder and approver agreements were not always maintained (see finding 2). Based on our interviews, review of supporting documentation, and testwork, we determined that purchases were adequately supported and recorded on the transaction logs; purchases appeared reasonable and necessary to conduct state business and did not exceed the single-purchase dollar limit; purchases complied with the Department of General Services' *Agency Purchasing Procedures Manual*; and payment card transaction logs were properly approved and reconciled to the statements.

**2. Staff did not always follow the state's policies and procedures for payment cards, which increases the risk of fraudulent activity**

**Finding**

The Department of Finance and Administration (F&A) implemented the State Payment Card system in March 2002 to provide departmental personnel an alternative payment method for small purchases. In order to establish the procedures for this program, F&A published the *State of Tennessee State Payment Card Cardholder/Approver Manual* (Cardholder/Approver Manual). The Department of Agriculture is required to maintain specific cardholder documentation, which

includes the State Payment Card New Account Application and Maintenance Forms, Cardholder Agreements, Approver Agreements, and Acknowledgement of Receipt forms. The agency coordinator did not maintain the specific cardholder documentation for new cardholders as follows:

- Supervisors did not sign 2 of 25 State Payment Card New Account Application and Maintenance Forms tested (8%), while the division directors did not sign 16 of the 25 forms tested (64%).
- The agency coordinator did not maintain Cardholder Agreements on file for 7 of 25 new cardholders tested (28%). Also, the agency coordinator did not sign the 18 Cardholder Agreements tested.
- The agency coordinator did not maintain Approver Agreements on file for 8 of 25 new cardholders tested (32%). Also, the agency coordinator did not sign the 17 Approver Agreements tested.
- There were no Acknowledgement of Receipt forms on file for 5 of 19 new cardholders tested (26%). Also, the approvers did not sign 3 of 14 Acknowledgement of Receipt forms tested (21%). The Acknowledgement of Receipt form does not apply to every cardholder. In June 2006, the state payment card contract was awarded to a new vendor; therefore, new payment cards were issued to all cardholders. However, a temporary payment card was initially issued. The Acknowledgement of Receipt form was used to document that the cardholder received this temporary payment card. In September 2006, the cardholders received the permanent payment card from the new vendor. So, if a new cardholder initially received the permanent payment card, the Acknowledgement of Receipt form would not apply.

The guidelines for payment card documentation are outlined in a September 2006 memo to agency coordinators and fiscal officers from F&A and the Cardholder/Approver Manual. The memo states:

Agency Fiscal Office must maintain on file the following documentation for each cardholder with an open account:

1. The original application for the cardholder's account
2. The signed Cardholder Agreement (FA-1000 09/06)
3. Signed Approver Agreements (FA-0999 09/06) from the cardholder's primary approver and any designated backup approvers
4. The original Acknowledgement of Receipt signed by the cardholder and approver upon receipt of the temporary Citibank Card

Also, according to Section 2.1 of the September 2006 version of the Cardholder/Approver Manual, the State Payment Card New Account Application and Maintenance Form "must be signed by the employee and the Cardholder's division authority."

In performing this testwork, we also noted that four individuals had active accounts, as of February 14, 2007, even though three were not current employees and one was not issued the payment card. We determined that no purchases had been made using these active accounts after the employees left the department, and no purchases were made against the open account where a payment card was not issued.

After discussing these issues with the agency coordinator and fiscal director, new Cardholder and Approver Agreements were obtained for the active cardholders who had missing forms, and the four inappropriate active accounts were closed.

We also asked some general questions of every cardholder located at Ellington Agricultural Center about their purchases and their compliance with the cardholder manual. Two cardholders stated that they had loaned their assigned payment card to another person and that not all purchases were made by the authorized cardholders. The Cardholder Agreement states, "I will not allow any other person to use the card," and states that improper usage includes "allowing someone else to use the card assigned to me." One of these cardholders admitted that he had allowed another authorized cardholder to use his card for a couple of purchases years ago, while the other cardholder admitted that he allowed his employees, who are not authorized cardholders, to use his card on a repetitive basis. Although the purchases we reviewed appeared appropriate for business purposes, loaning payment cards to unauthorized employees increases the risk of fraud or abuse in payment card transactions and should never be permitted.

We tested several nonstatistical samples of payment card transactions made during the audit period for adequate documentation, reconciliation to the transaction logs, and compliance with the Department of General Services' *Agency Purchasing Procedures Manual*. We found no problems.

### **Recommendation**

The fiscal director should ensure that the agency coordinator is maintaining all of the required cardholder documentation. The fiscal director should develop a process by which Fiscal Services is promptly informed when employees leave the department. Also, the fiscal director and agency coordinator should reemphasize to payment card cardholders that they are not to allow anyone else including other authorized cardholders to use the payment card that has been assigned to them. The Commissioner should ensure that appropriate disciplinary action is taken for cardholders who fail to follow established guidelines and controls related to the payment card process.

In addition, the Commissioner should ensure that other risks of improper accountability, noncompliance, fraud, waste, or abuse are adequately identified and assessed in management's documented risk assessment. Management should implement effective controls to ensure compliance with applicable requirements and should assign staff to be responsible for ongoing monitoring of the risks and mitigating controls and take action if deficiencies occur.

## **Management's Comment**

We concur. The agency coordinator has already obtained all missing documentation and has filed it in books. The agency coordinator will continue to maintain all necessary documentation as new employees receive payment cards. The fiscal director will work with the human resources director to develop a process by which Fiscal Services is promptly informed when employees leave the department. An exit checklist has already been developed that should help with this process.

The fiscal director and the agency coordinator will continually emphasize to cardholders that they are not allowed to give their payment cards to any other person. The Commissioner will ensure that appropriate disciplinary action is taken for cardholders who fail to follow established guidelines and controls related to payment cards.

The Department has recently hired an internal auditor. The internal auditor will audit a sample of payment card transactions each month to help ensure that any noncompliance, fraud, waste or abuse is identified. If such cases occur, action will be taken to correct these deficiencies.

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## **EQUIPMENT**

Our objectives for reviewing equipment controls and procedures were to determine whether

- equipment was adequately safeguarded;
- the annual equipment inventory process was completed;
- equipment information was correctly recorded in the Property of the State of Tennessee (POST) system;
- equipment could be located or confirmed;
- access to POST was appropriate;
- lost or stolen equipment was removed from POST; and
- vehicles and equipment leased from Motor Vehicle Management (MVM) could be located.

We interviewed key department personnel and reviewed supporting documentation to gain an understanding of the department's policies, procedures, and controls over equipment; to determine whether equipment was adequately safeguarded; and to determine if the annual inventory process was completed. We selected nonstatistical samples of equipment to determine whether the equipment information in POST was correct and whether equipment could be located or confirmed. Equipment information reviewed included state tag number, description, location, and serial number. We selected for testwork items at the Ellington Agricultural Center

and multiple forestry offices and buildings across the state. We obtained a listing of those individuals with access to POST as of January 12, 2007. We tested the individuals on the listing to determine whether they were employees of the department as of the date of the listing, whether they had job duties that required their designated level of access, and whether this level of access created an inadequate segregation of duties. We reviewed the listing of equipment from POST to determine whether lost or stolen equipment had been removed from POST. We obtained from MVM a listing dated January 4, 2007, of all vehicles and equipment being leased by the department. We selected a nonstatistical sample to determine whether the leased vehicles and equipment could be located.

Based on our interviews and observations, we determined that equipment was adequately safeguarded. Based on our testwork, we determined that equipment information was properly recorded in POST, with minor exceptions, and that access to POST was appropriate. Lost or stolen equipment had been removed from POST. Also, based on our testwork, we determined that vehicles and equipment leased from MVM could be located. However, we determined that the annual equipment inventory process was not completed for 2006 and that some equipment items could not be located (see finding 3).

**3. The property officer did not complete the equipment inventory process, which increases the risk that loss or theft of equipment items will not be detected timely**

**Finding**

The department uses the Property of the State of Tennessee (POST) system to maintain information on its equipment, such as descriptions, serial numbers, state tag numbers, etc. According to General Services' *POST Users Manual*, "each state agency must take an annual physical inventory prior to the close of the fiscal year. The Department of General Services establishes the date(s) that each department completes their inventory." The department's property officer is responsible for completing the annual inventory by June 30 each year. However, as of July 13, 2006, according to POST, 897 of the department's 4,682 equipment items (19%) had not been inventoried for 2006. Most of the items had last been inventoried in 2004 or 2005; however, some had not been inventoried as long ago as 1999. The total acquisition cost of the 897 items was \$2,158,604.

To aid in the completion of the annual inventory, a department may request from General Services an exception report which lists all of the department's equipment shown in POST that has not been inventoried in the current year. A property officer may request this report after completing 50% of the inventory. The department requested and reviewed the exception reports for the years ended June 30, 2005, and June 30, 2004. However, the property officer did not request the exception report for the June 30, 2006, inventory until February 2007, because he incorrectly thought that 90% of the inventory had to be complete before the exception report could be requested.

Testwork performed on a sample of 50 equipment items listed in POST revealed that 4 items could not be located (8%). These items were two printers, a two-way radio, and a modem, totaling \$726.03. According to POST, three of these items had not been inventoried since 2001.

Without the completion of the annual inventory, the department cannot ensure that its equipment inventory records are accurate. Furthermore, there is an increased risk that loss or theft of the state's equipment will not be prevented or detected timely when proper accountability for equipment is not enforced.

### **Recommendation**

The fiscal director should ensure that the property officer is performing all the steps in the inventory process to accomplish a complete and accurate inventory count. The property officer should follow up any concerns with inventory results and should resolve any issues completely and promptly so that he can update POST and report missing items to the Comptroller's Office as required. The property officer needs to request the exception report from General Services timely each year to aid in the inventory count.

In addition, the Commissioner should ensure that other risks of improper accountability, noncompliance, fraud, waste, or abuse are adequately identified and assessed in management's documented risk assessment. Management should implement effective controls to ensure compliance with applicable requirements and should assign staff to be responsible for ongoing monitoring of the risks and mitigating controls and take action if deficiencies occur.

### **Management's Comment**

We concur. The fiscal director will ensure that the property officer is performing all steps in the inventory process. The fiscal director will make sure the property officer understands the need to follow up any concerns with inventory results and resolve issues completely and promptly. The property officer will update POST and report any missing items to the Comptroller's Office. The property officer will also request the exception report from General Services in a timely manner each year.

Any weaknesses in equipment procedures will be noted in the Department's risk assessment. Management will implement effective controls to ensure compliance with requirements. Appropriate action will be taken when necessary to correct deficiencies.

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## EXPENDITURES

Our objectives in reviewing expenditure controls and procedures were to determine whether

- payments for travel were made in accordance with the State of Tennessee Comprehensive Travel Regulations;
- revenue and expenditure transactions between state agencies were made in accordance with the Department of Finance and Administration's (F&A's) Policy 18, *Journal Vouchers–Type J*;
- access to the State of Tennessee Accounting and Reporting System (STARS), the Tennessee On-Line Purchasing System (TOPS), and the State Employee Information System (SEIS) was appropriate;
- payments made on Z-type contracts were after the contracts were fully approved; and
- payroll overpayments were handled in accordance with F&A Policy 11, *Recovery of Overpayments and Other Debts Owed by Employees to the State*.

We interviewed key department personnel and reviewed supporting documentation to gain an understanding of the department's policies and procedures over expenditures. We tested a nonstatistical sample of travel expenditures to determine whether the payments were made in accordance with the Comprehensive Travel Regulations. The State of Tennessee uses J-type journal vouchers to record revenue and expenditure transactions between state agencies. The Department of Finance and Administration has developed Policy 18 to provide guidance on recording these transactions between state agencies. We selected a nonstatistical sample of revenue transactions and a nonstatistical sample of expenditure transactions for the department to determine whether the Department of Agriculture recorded these transactions in accordance with Policy 18. We accessed the accounting, purchasing, and payroll systems to determine which employees were recognized users and to determine these employees' level of access. We tested the entire population and determined if the persons were employees of the department, had job duties which required their designated level of access, and whether this level of access created an inadequate segregation of duties. In order to be a fully approved contract for the State of Tennessee, the Commissioner for the Department of Finance and Administration has to approve the contract. In order to expedite this process, the Department of Finance and Administration can authorize departments to issue fully approved contracts through a departmental grant authority (DGA). All contracts issued pursuant to a DGA are considered to be Z-type contracts. We selected a nonstatistical sample of Z-type contracts and compared the initial payments to the approval dates on the contracts to determine whether the payments were after the contracts were fully approved. We selected all overpayments to employees to determine whether payroll overpayments were handled in accordance with F&A Policy 11.

Based on our testwork, we determined that payments for travel were made in accordance with the Comprehensive Travel Regulations; revenue and expenditure transactions between state agencies were made in accordance with F&A Policy 18, with minor exceptions; access to STARS, TOPS, and SEIS was appropriate; payments on Z-contracts were after the contracts were fully approved; and payroll overpayments were handled in accordance with F&A Policy 11, with a minor exception.

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## **DEPARTMENT OF FINANCE AND ADMINISTRATION POLICY 16—*EMPLOYEE HOUSING AND MEALS***

The Department of Agriculture has employees working at state forests, work centers, and fire towers around the state who are required to live nearby in order to be able to respond to emergencies. The department places these employees in state-owned housing.

On January 30, 1998, the Department of Finance and Administration (F&A) issued Policy 16, *Employee Housing and Meals*; F&A revised the policy in April 2007. This policy was issued to establish guidelines which ensure compliance with applicable state and federal laws, particularly Internal Revenue Code requirements, governing all housing and meals provided to all officials and employees and to provide a uniform policy addressing all state-owned housing.

Our objectives in reviewing compliance with Policy 16 were to determine whether

- the department had procedures in place which ensured that F&A Policy 16 was followed;
- the department's housing plan was approved by F&A;
- the department's housing plan contained the information required by Policy 16;
- employees living in state-owned housing had completed the required forms; and
- employees living in state-owned housing did not receive a housing allowance.

We reviewed Policy 16 to gain an understanding of its requirements. We interviewed key department personnel and reviewed supporting documentation to gain an understanding of the procedures they used to ensure compliance with the requirements of the policy. We obtained the department's housing plan and reviewed the plan to determine whether the plan had been approved by F&A and contained the information required by Policy 16. Policy 16 requires the plans to include "the employee's name, social security number, location of the housing, square footage of the dwelling, calculated monthly rent amount, justification of the housing assignment, and if applicable, approved Employee Housing Disclosure Forms." We tested every employee listed in the approved plan to determine if the forms required by Policy 16 had been completed. We interviewed key department personnel to determine if any employees living in state-owned housing also received a housing allowance.

Based on interviews and review of supporting documentation, we determined that the department had procedures in place to ensure compliance with F&A Policy 16; the department's

housing plan was approved by F&A; and the department's housing plan contained the information required by Policy 16. Based on the testwork performed, we concluded that the department's employees had completed all required forms and that none of the employees living in state-owned housing also received a housing allowance.

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## **REGULATORY SERVICES**

Our objectives for reviewing the controls and procedures in the Regulatory Services Division were to determine whether the policies and procedures were documented and adequate.

We interviewed key department personnel and reviewed supporting documentation to gain an understanding of the department's policies, procedures, and controls in the Regulatory Services Division. This inquiry included the following program areas: Animal Health, Food and Dairy, Pesticides, and Plant Certification. Based on our interviews and reviews of supporting documentation, we determined that the policies and procedures were documented and adequate.

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## **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 objective was to determine whether the department's June 30, 2006; June 30, 2005; and June 30, 2004, responsibility letters were filed in compliance with Section 9-18-104, *Tennessee Code Annotated*.

Although the responsibility letters had been prepared and were on file at the department, none of the three letters could be found at the Comptroller's Office and only the June 30, 2004, letter could be found at the Department of Finance and Administration.

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## **OBSERVATIONS AND COMMENTS**

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### **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, *Consideration of Fraud in a Financial Statement Audit*, 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, 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.

## **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 Agriculture filed its compliance reports and implementation plans on August 2, 2006; September 15, 2005; and September 15, 2004.

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

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## **APPENDIX**

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### **ALLOTMENT CODES**

325.01	Administration and Grants
325.04	Forestry Seasonal Payroll
325.05	Division of Regulatory Services
325.06	Marketing Development and Promotion
325.08	Agricultural Resources Conservation Fund
325.10	Forestry Operations
325.11	Forestry Facility Maintenance
325.12	Tennessee Grain Indemnity Fund
325.14	Certified Cotton Growers' Organization
325.16	Tennessee Agricultural Regulatory Fund