AUDIT REPORT

General Assembly
Fiscal Review Committee

October 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
Nashville, Tennessee 37243-0260
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John G. Morgan
Comptroller

October 30, 2007

The Honorable Ron Ramsey
Speaker of the Senate
and
The Honorable Jimmy Naifeh
Speaker of the House of Representatives
and
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243
and
Mr. James W. White, Executive Director
Fiscal Review Committee
320 Sixth Avenue North, 8th Floor
Nashville, Tennessee 37243

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Fiscal Review Committee for the period April 24, 2004, through June 30, 2007.

The review of internal control and compliance with laws and regulations resulted in no audit findings.

Sincerely,

John G. Morgan
Comptroller of the Treasury

JGM/to
07/107

STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
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July 17, 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 Fiscal Review Committee for the period April 24, 2004, through June 30, 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 Fiscal Review Committee's compliance with laws, regulations, and provisions of contracts or grant agreements significant to the audit objectives. Management of the Fiscal Review Committee 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 resulted in no audit findings.

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
Fiscal Review Committee
October 2007

AUDIT SCOPE

We have audited the Fiscal Review Committee for the period April 24, 2004, through June 30, 2007. Our audit scope included a review of internal control and analytical procedures in the areas of expenditures and payroll and personnel. The audit was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States.

AUDIT FINDINGS

The audit report contains no findings.

Financial and Compliance Audit
Fiscal Review Committee

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INTRODUCTION

POST-AUDIT AUTHORITY

This is the report on the financial and compliance audit of the Fiscal Review Committee. 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.

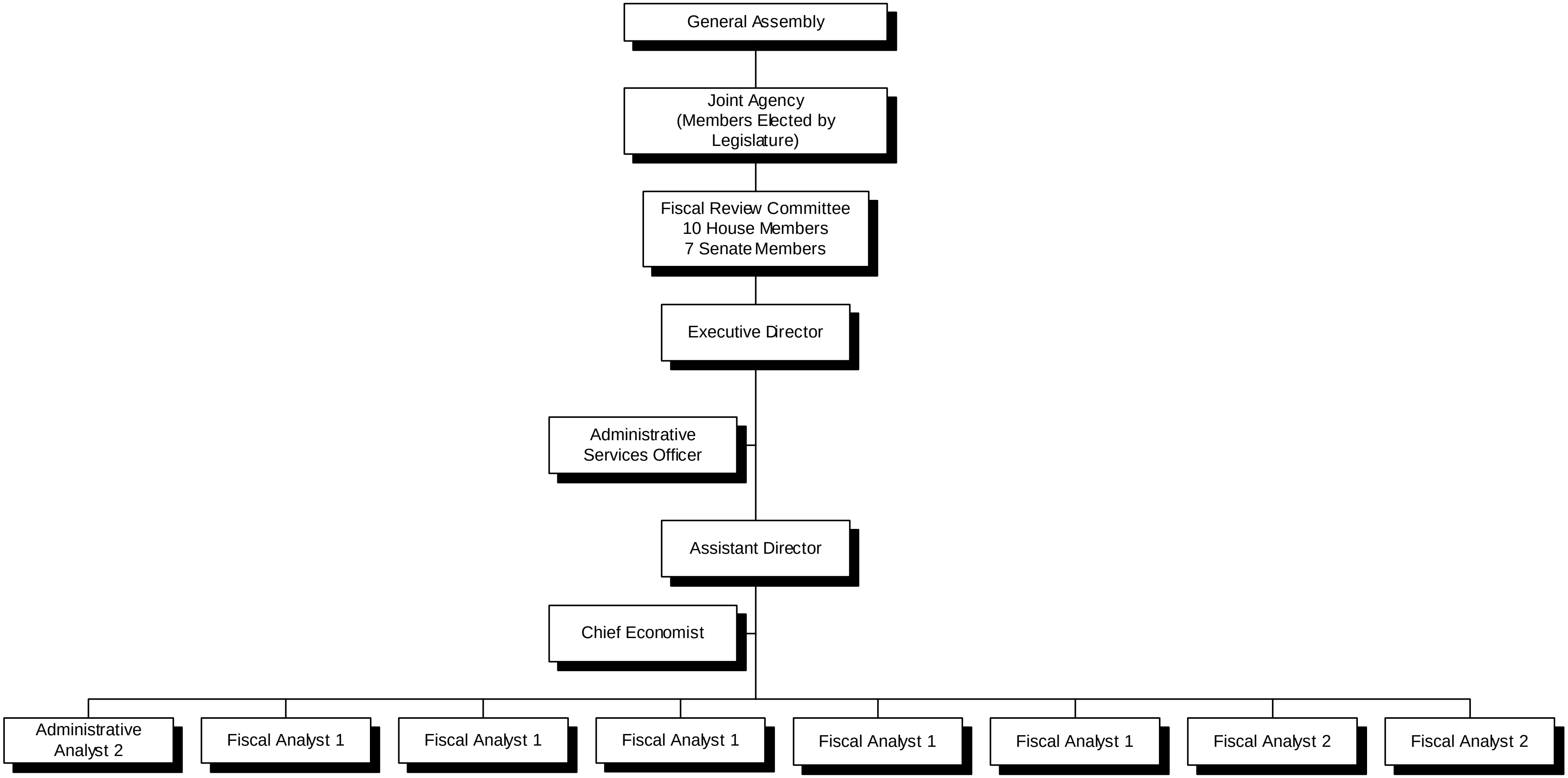
BACKGROUND

The Eighty-fifth General Assembly established the Fiscal Review Committee in 1967 as a special, continuing committee to keep the members of the legislature informed of the fiscal matters of the State of Tennessee. The committee is composed of six senators and nine representatives elected by their respective houses; the speakers of both houses; and the chairs of the Finance, Ways and Means Committees of both houses. The Comptroller of the Treasury serves as secretary and is directed to furnish staff as required.

The Fiscal Review Committee conducts a continuing review of the fiscal operations of state government. The committee is responsible for preparing and distributing the fiscal notes required by Section 3-2-107, *Tennessee Code Annotated*. With the Comptroller and the Commissioner of Finance and Administration, the committee is responsible for reviewing, at least annually, the organization and operation of state government to determine if changes are needed.

The Fiscal Review Committee is accounted for in allotment code 301.05. An organization chart of the committee is on the following page.

Fiscal Review Committee
Organization Chart



AUDIT SCOPE

We have audited the Fiscal Review Committee for the period April 24, 2004, through June 30, 2007. Our audit scope included a review of internal control and analytical procedures in the areas of expenditures and payroll and personnel. The audit was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States.

PRIOR AUDIT FINDINGS

There were no findings in the prior audit report.

OBJECTIVES, METHODOLOGIES, AND CONCLUSIONS

EXPENDITURES

Our objectives in the review of expenditures were to

- consider management's overall internal control environment in planning the audit and preparing the written audit program,
- obtain a general knowledge of the types and amounts of annual expenditures,
- detect unusual or unexpected patterns or trends in expenditures,
- determine propriety of transaction authorization, and
- determine that expenditure reports received from the Department of Finance and Administration were reconciled with the committee's voucher registers.

We interviewed key employees, reviewed the organization chart, examined relevant correspondence received, and considered management's overall control environment. We also interviewed key employees to gain and document the types and amounts of annual expenditures. Reports comparing current-year actual expenditures to prior-year actual expenditures and actual expenditures to budgeted expenditures for each fiscal year were obtained from the Division of State Audit's Information Technology staff. These reports were analyzed, and significant variances were discussed with the committee's administrative staff. Corroborating evidence for variances was obtained and reviewed. Voucher registers and other documentation regarding specific expenditure transactions were reviewed for proper authorization approval. We also reviewed the committee's reconciliations between expenditure reports received from the Department of Finance and Administration and the committee's voucher registers.

Based on our interviews, the review and analysis of reports of actual and budgeted expenditures, and review of supporting documentation for significant variances, the amounts and types of expenditures were in substantial conformity with budgeted expectations and no unexplained unusual or unexpected patterns or trends in expenditures occurred. Furthermore, expenditure transactions were properly authorized and reconciliations between Department of Finance and Administration reports and the committee's voucher registers were performed.

PAYROLL AND PERSONNEL

Our objectives in the review of payroll and personnel were to:

- consider management's overall internal control environment in planning the audit and preparing the written audit program, and
- perform analytical procedures to detect unusual or unexpected changes in payroll expenditures.

We interviewed key employees, reviewed the organization chart, examined relevant correspondence received, and considered management's overall control environment. Reports of actual and budgeted payroll expenditures for each fiscal year were obtained from the Division of State Audit's Information Technology staff. The reports were analyzed, and significant variances were discussed with the committee's administrative staff. Corroborating evidence was obtained and reviewed.

Based on our interviews, the review and analysis of reports of actual and budgeted payroll, and review of supporting documentation for significant variances, it appears that the amounts and types of payroll expenditures were in substantial conformity with budgeted expectations and no unexplained unusual or unexpected patterns or changes in payroll expenditures occurred.

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 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.