

AUDIT REPORT

Tennessee Commission on Children and Youth

May 2009



STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY

Department of Audit
Division of State Audit



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May 21, 2009

The Honorable Phil Bredesen, Governor

and

Members of the General Assembly

State Capitol

Nashville, Tennessee 37243

and

Members of the Tennessee Commission on

Children and Youth

and

Ms. Linda O'Neal, Executive Director

Tennessee Commission on Children and Youth

Andrew Johnson Tower, Ninth Floor

710 James Robertson Parkway

Nashville, Tennessee 37243

Ladies and Gentlemen:

We have conducted a financial and compliance audit of selected programs and activities of the Tennessee Commission on Children and Youth for the period June 1, 2005, through May 31, 2008.

We conducted our audit in accordance with generally accepted government auditing standards. These standards require that we obtain an understanding of internal control significant to the audit objectives and that we design the audit to provide reasonable assurance of the Tennessee Commission on Children and Youth's compliance with laws, regulations, and provisions of contracts or grant agreements significant to the audit objectives. Management of the Tennessee Commission on Children and Youth is responsible for establishing and maintaining effective internal control and for complying with applicable laws, regulations, and provisions of contracts and grant agreements.

May 21, 2009
Page Two

Our audit disclosed certain findings which are detailed in the Objectives, Methodologies, and Conclusions section of this report. The commission'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 commission's internal control and instances of noncompliance to the Tennessee Commission on Children and Youth's management in a separate letter.

Sincerely,

A handwritten signature in black ink that reads "Arthur A. Hayes, Jr." with a stylized flourish at the end.

Arthur A. Hayes, Jr., CPA
Director

AAH/cj
08/039

State of Tennessee

Audit Highlights

Comptroller of the Treasury

Division of State Audit

Financial and Compliance Audit
Tennessee Commission on Children and Youth
May 2009

AUDIT SCOPE

We have audited the Tennessee Commission on Children and Youth for the period June 1, 2005, through May 31, 2008. 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 revenue, expenditures, grants and contracts, payment cards, and the Financial Integrity Act. The audit was conducted in accordance with generally accepted government auditing standards.

AUDIT FINDINGS

The Tennessee Commission on Children and Youth Used an Unauthorized Bank Account, and the Controls Over the Account Were Inadequate, Which Increased the Risk of Fraud and Abuse

The commission's Executive Director and staff used an unauthorized bank account to conduct state business and, in doing so, circumvented state policies and procedures, including state purchasing guidelines. In addition, the Executive Director and staff did not ensure that controls over the unauthorized account were adequate, which increased the risk of fraud and abuse associated with the account. Specifically, the Executive Director and staff did not segregate duties for handling the account; did not ensure that bank statements were reconciled to the commission's records; did not monitor account activity related to the commission's business; and did not ensure compliance with the Department of Finance and Administration's Policy 7, *Petty Cash and Departmental Bank Accounts* (page 6).

The Commission Failed to Implement Adequate Controls Over Monitoring of Grant Contracts, Increasing the Risk That Noncompliance With Contract Provisions Could Occur and Not Be Detected*

As stated in the prior audit, the commission's controls over monitoring of the grant contracts awarded to local governments and other agencies were not adequate to ensure compliance with state and federal monitoring guidelines. The commission did not monitor all of the grants its monitoring plan required it to monitor. As a result, the commission did not comply with the Department of Finance and Administration's Policy 22, *Subrecipient Contract Monitoring* (page 13).

*This finding is repeated from the prior audit.

Financial and Compliance Audit Tennessee Commission on Children and Youth

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Financial and Compliance Audit Tennessee Commission on Children and Youth

INTRODUCTION

POST-AUDIT AUTHORITY

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

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

BACKGROUND

The Tennessee Commission on Children and Youth is an independent state agency created by the Tennessee General Assembly. Its primary mission is advocacy for improvement in the quality of life for the state’s children and families. To fulfill this mission, staff of the Tennessee Commission on Children and Youth gather, analyze, and report information on children and families for the planning and coordination of policies, programs, and services. The commission evaluates selected state programs and services for children.

The commission’s policymaking body is a 21-member board appointed by the Governor and consists of people active in addressing the problems and needs of children and youth. At least one member is selected from each of the state’s nine development districts, and the commissioners, or their designees, of state departments serving children serve *ex officio*. Five youth advisory members serve on the commission to meet the federally mandated composition required for a state advisory group.

Advocacy

The commission provides leadership for advocacy activities on behalf of children and families. The commission is an integral part of state policymaking on child and family issues and participates on national, state, regional, and local committees, task forces, and boards for information gathering, sharing, and networking.

Regional Councils

The commission staffs and coordinates nine regional councils that provide organizational structure for statewide networking on behalf of children and families. The councils address the needs of children and families at the regional level and offer local-level feedback to the commission.

Information Dissemination

The commission gathers, analyzes, and reports information on children and families in various publications, such as *KIDS COUNT: The State of the Child in Tennessee*, an annual county-by-county picture of the condition of children; *The Advocate*, a periodic newsletter sent to legislators, policymakers, children's advocates, service providers, and regional council members; and *Tennessee Compilation of Selected Laws on Children, Youth, and Families*, distributed to juvenile courts, state government staff, and other children's services professionals.

Juvenile Justice

The commission is the state advisory group responsible for implementing provisions of the Juvenile Justice and Delinquency Prevention (JJDP) Act. The JJDP funds are awarded as Federal Formula and Title V grants. The Federal Formula grants are awarded to local governments or other organizations for delinquency prevention and to ensure that youth who commit offenses receive appropriate placements and services. The Title V grants are awarded to local governments to promote collaboration within communities for developing delinquency prevention strategies.

The commission also administers the Juvenile Accountability Block Grant (JABG) and the Enforcing Underage Drinking Laws (EUDL) program. The JABG funds are used to promote greater accountability in Tennessee's juvenile justice system and for juveniles who commit criminal offenses. The EUDL program is designed to reduce the availability and consumption of alcoholic beverages by minors.

The commission awards Court Appointed Special Advocate (CASA) grants to local CASA programs to support and promote court-appointed volunteer advocacy for abused and neglected children so that they can thrive in safe, permanent homes. The commission also administers the state supplements and reimbursement account for juvenile court services improvement as authorized by Section 37-1-162, *Tennessee Code Annotated*. The state supplements for improving juvenile courts require each court to have at least a part-time youth services officer in order to receive the funding. The reimbursement account assists counties in paying for alternatives to placing youth in adult jails.

Evaluation of Services for Children

The commission conducts targeted evaluations and is responsible for the Children's Program Outcome Review Team (CPORT) evaluation. CPORT utilizes a quality service review methodology to provide an independent determination of the status of children in state custody and their families and how well the service system is performing to meet their needs.

Ombudsman Program

The Ombudsman Program has a staff that serves as neutral reviewers to respond to questions, concerns, or complaints regarding children in state custody. Ombudsman staff have been trained and certified as mediators to work toward resolution of issues in the best interest of the child and family and community safety.

The Tennessee Commission on Children and Youth is part of the general fund of the State of Tennessee (allotment code 316.01). An organization chart of the commission is on the following page.

AUDIT SCOPE

We have audited the Tennessee Commission on Children and Youth for the period June 1, 2005, through May 31, 2008. 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 revenue, expenditures, grants and contracts, payment cards, and the Financial Integrity Act. The audit was conducted in accordance with generally accepted government auditing standards.

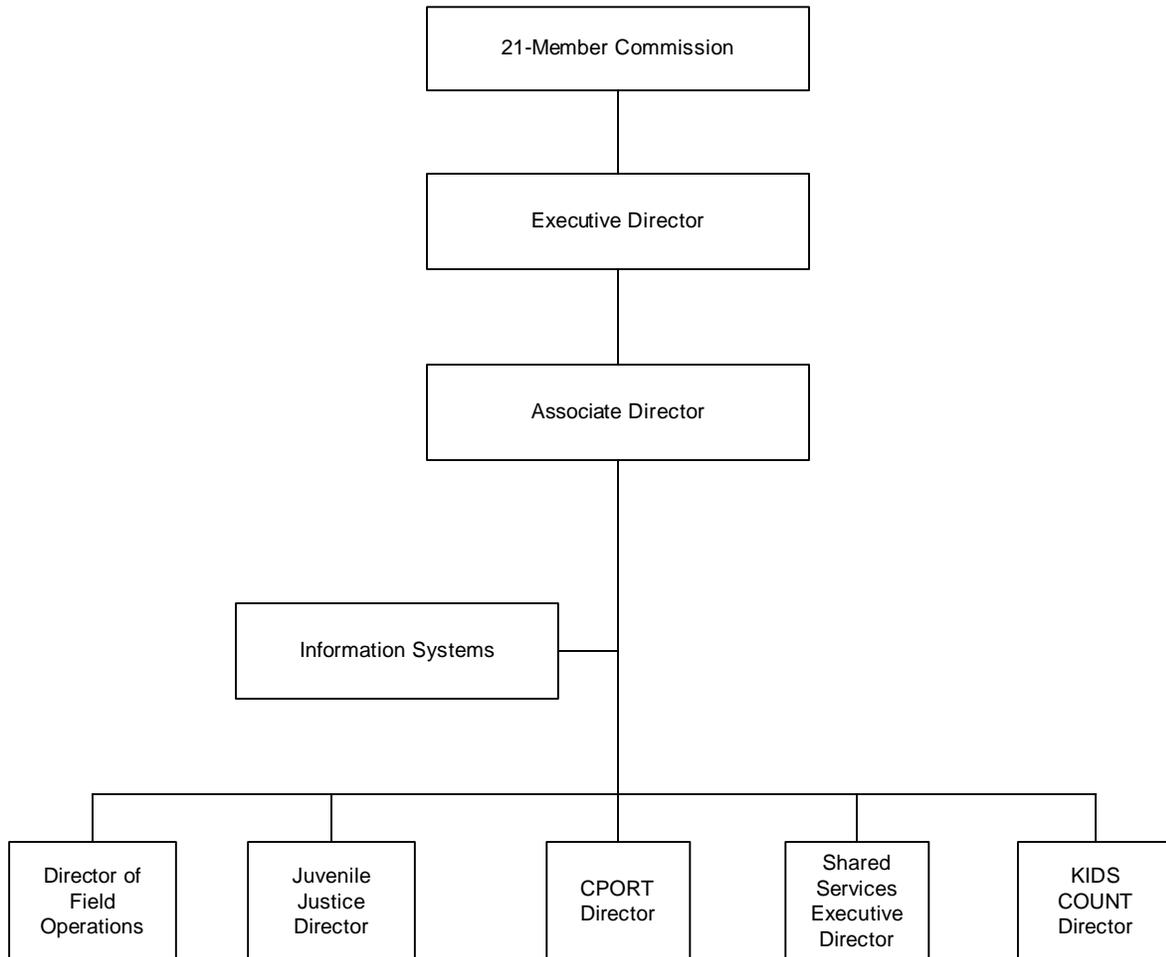
PRIOR AUDIT FINDINGS

Section 8-4-109, *Tennessee Code Annotated*, requires that each state department, agency, or institution report to the Comptroller of the Treasury the action taken to implement the recommendations in the prior audit report. The Tennessee Commission on Children and Youth filed its report with the Department of Audit on March 31, 2006. 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 Tennessee Commission on Children and Youth has corrected the previous audit finding concerning the verification of the educational background of external CPORT reviewers.

Tennessee Commission on Children and Youth Organization Chart



REPEATED AUDIT FINDING

The prior audit report also contained a finding concerning controls over monitoring of grant contracts. The finding has not been resolved and is repeated in the applicable section of this report.

OBJECTIVES, METHODOLOGIES, AND CONCLUSIONS

REVENUE

Our objectives for reviewing controls and procedures over revenue were to determine whether

- cash collected during the audit period was deposited timely and accounted for in the appropriate fiscal year;
- revenue transactions were adequately supported, charged to the proper source codes, and recorded at the correct amount; and
- the commission's revenue records were reconciled with the Department of Finance and Administration's (F&A) reports.

We interviewed key commission personnel and reviewed supporting documentation to gain an understanding of revenue internal controls including the procedures for collecting, recording, and depositing cash. We tested all cash receipts recorded from June 1, 2005, through February 1, 2008, and compared the detailed cash receipt with the corresponding deposit record to determine if cash collected during the audit period was deposited timely and accounted for in the appropriate fiscal year. As a result of the testwork performed, we determined that cash collected during the audit period was deposited timely, with minor exceptions, and was accounted for in the appropriate fiscal year.

We tested a nonstatistical sample of revenue transactions processed through the State of Tennessee Accounting and Reporting System (STARS) for the period June 1, 2005, through November 30, 2007, to determine if revenue transactions were adequately supported, charged to the proper source codes, and recorded at the correct amount. We examined journal vouchers and other related supporting documentation for each transaction tested. As a result of the testwork performed, we determined that revenue transactions were adequately supported, charged to the proper source codes, and recorded at the correct amount.

We interviewed key personnel to determine the commission's revenue reconciliation procedures and reviewed the revenue reconciliations for the audit period to determine if the commission's records were reconciled with F&A reports. Based on our review, we determined

that the commission's revenue records were not consistently reconciled with F&A reports during the audit period. Commission management disclosed that due to changes in their fiscal staff, including the retirement of the Fiscal Director and the subsequent decision to contract out accounting services, revenue records were not always reconciled with F&A reports from October 1, 2005, through June 30, 2007. The lapse in reconciliation procedures occurred prior to the contract for accounting services with F&A's Shared Services Solutions unit on July 1, 2007. After July 1, 2007, the commission's revenue records were reconciled with F&A reports.

During our testwork on revenues, we discovered that the commission had been using an unauthorized bank account to conduct state business. The Executive Director originally established the bank account as an employee account; however, as discussed in finding 1, the commission began using this account to deposit sponsorship fees and pay certain expenses for its annual conference. We obtained and reviewed the commission's records for the revenues received and expenses incurred for the annual conference for the years 2005, 2006, 2007, and 2008 to determine if the sponsorship money collected from the annual conference was properly accounted for by the commission. We found that the controls over the bank account were inadequate, as discussed in finding 1.

1. The Tennessee Commission on Children and Youth used an unauthorized bank account, and the controls over the account were inadequate, which increased the risk of fraud and abuse

Finding

The Tennessee Commission on Children and Youth's (TCCY) Executive Director and staff used an unauthorized bank account to conduct state business. The Executive Director originally established the bank account as an employee account; however, as discussed below, the commission began using this account to deposit sponsorship fees and pay expenses for its annual conference. By using this account, the commission circumvented state policies and procedures, including state purchasing guidelines. In addition, the Executive Director and staff did not ensure that controls over the unauthorized account were adequate, which increased the risk of fraud and abuse associated with the account. The Executive Director stated that she did not consider the sponsorship fees state funds, and therefore, she did not think she had to follow the state's policies and procedures.

In 1999, the Executive Director opened a personal checking account for use by the commission's employees. According to the Executive Director, a "Sunshine Fund" (also referred to as the account) was created to deposit employees' voluntary annual contributions which could be used to purchase flowers, cards, or gifts to recognize important times or events in the lives of the commission's employees, such as birthdays, retirements, illnesses, or deaths. At this time, the checking account was appropriately considered to be a non-state funds account and exempt from the Department of Finance and Administration's (F&A) Policy 7, *Petty Cash and Departmental Bank Accounts*, since it contained no state funds. However, several years ago (the exact date is unknown by TCCY staff), the Executive Director and TCCY staff began using the

Sunshine Fund to deposit sponsorship fees and to pay expenses for the commission's annual Children's Advocacy Days (CAD), which is a state event. The Children's Advocacy Days is an annual two-day conference which provides a forum for state employees and other non-state individuals working with, and on behalf of, children and families across the state. The conference's mission is to provide individuals with new information that will facilitate their efforts to improve the lives of children and families in their communities. When the Executive Director decided to use the Sunshine Fund to deposit money collected from sponsors supporting the CAD, the bank account became subject to F&A Policy 7.

F&A Policy 7, Section 07-02-101, states that when "funds obtained by state employees or agents in the course of their state employment" are placed in a bank account, "the bank accounts are state funds and are subject to this policy statement and all applicable laws, rules and regulations pertaining to state funds." Furthermore, F&A Policy 7, Section 07-02-102.D.2, describes a departmental operating account as a type of account that is used in an operation where fees generated from the operation are deposited into the account and disbursements in support of the operation are made from the account. Since the sponsorship fees are collected by state employees and generated from a state event, we believe the sponsorship fees are state funds.

Section 07-02-101 also states "any account which consists of non-state funds should not have any reference to the State of Tennessee or any subdivision thereof in the account name, and no state funds shall be deposited in such accounts under any circumstances." The Executive Director's name is on the checking account followed by "TCCY Sunshine Fund," as confirmed during our review of the bank statements for the account. Having the commission's name in the account title is further evidence that the account should be considered a state account. The checks themselves list the Executive Director's name, the fund custodian's name, and a former employee's name. These were the three authorized check signers on the account, although only one was required to sign a check.

The custodian of the TCCY Sunshine Fund is the commission's Information Systems Specialist. Since the fund contained contributions from sponsors of CAD and contributions from employees (the original intent of the fund), proper accounting for each type of contribution should have been maintained; however, this was not done. To account for the activity of the CAD portion of the fund, the fund custodian maintained records for each calendar year showing the beginning CAD balance, deposits into the account for CAD, withdrawals from the account for CAD, and the ending CAD balance. The custodian did not maintain a record of activity for the employee portion of the fund; therefore, the custodian considered the difference between the actual bank balance and the CAD balance per his records as the amount of the fund that belonged to the employees. As confirmed by the bank, the TCCY Sunshine Fund checking account balance was \$1,999.51 as of March 31, 2008. According to the records maintained by the fund custodian, \$950.25 was the CAD balance, leaving \$1,049.26 belonging to the TCCY employees. However, as noted below, the custodian's records were not always accurate.

On July 1, 2007, F&A's Office of Shared Services Solutions began providing fiscal and procurement services to the commission. The office recommended that CAD sponsorship fees be deposited into and CAD expenses be paid from an official state bank account. For the 2008

CAD, sponsorship fees were deposited into and most expenses were paid from an official state bank account. However, according to the commission's records, in March 2008, the commission also paid \$427.32 for wine and \$300.00 for entertainment for the 2008 CAD legislative reception from the remaining CAD funds in the Sunshine Fund checking account.

Based on our discussions with commission staff and examination of the supporting documentation available including bank statements, invoices, and carbon copies of the checks in the checkbook, we determined that the custodian had been granted complete and sole control over the checking account by the Executive Director. Specifically, the custodian was responsible for paying all expenses by writing and signing checks, collecting and depositing all receipts, and maintaining physical control over the checkbook. None of the invoices or receipt and deposit records we reviewed contained evidence of review or approval by the Executive Director or any other employee.

We noted that the Executive Director had not assigned the responsibility of performing bank reconciliations to anyone, nor did she perform them herself. When bank statements are not reconciled, the possibility of fraud and errors is increased. In our review, we identified several problems (described below) that the Executive Director or other assigned members of management would have found had they adequately monitored the account operations and the fund custodian's activities and reconciled the bank statements on an ongoing basis.

Based on the information disclosed by management about the TCCY Sunshine Fund account and the increased risks of fraud and abuse associated with the actual use of the account, we reviewed all account transactions for the period January 1, 2005, through March 31, 2008, and found the following problems:

- The fund custodian did not retain invoices to support all expenses paid from the fund. In 2005, according to the bank statements, ten checks totaling \$8,948.42 cleared the bank; however, the fund custodian was only able to provide invoices or other supporting documentation for four of those checks totaling \$8,252.01, leaving an unsupported difference of \$696.41. In 2006, the bank statements showed that ten checks totaling \$13,613.81 had cleared the bank; however, the fund custodian was only able to provide invoices or other supporting documentation for six of those checks totaling \$13,391.41, leaving a difference of \$222.40. In 2007, the bank statements indicated that 21 checks totaling \$15,549.68 had cleared the bank; however, the fund custodian was only able to provide invoices or other supporting documentation for four of those checks totaling \$2,426.39, leaving an unsupported difference of \$13,123.29. Because of the increased fraud risk due to an increased number of missing invoices in 2007, we decided to confirm the unsupported 2007 expenses shown on the custodian's CAD records directly with the vendors. Vendors were able to provide supporting invoices for an additional eight checks totaling \$12,184.73, leaving a remaining balance of \$938.56 unsupported and unconfirmed. (According to the custodian's records of expenses, carbon copies of the checks, and discussions with employees, \$463.88 of the \$938.56 was reimbursements to employees for purchases they had made on the commission's behalf—\$166.24 for

food and decorations for CAD, \$117.64 for employee cakes and flowers, and \$180.00 for gift cards to be given as prizes or gifts at the commission's annual fall retreat. We were unable to confirm who received the gift cards. Also included in the \$938.56 were payments of \$365.42 to a liquor store for wine for the CAD legislative reception and \$109.26 to a florist for employee flowers.)

- The fund custodian did not keep detailed deposit slips to differentiate collections from employees and collections from conference sponsors; therefore, we could not reconcile receipt records with the bank statements to ensure that all money received for the conference had been deposited. The bank statements showed total deposits of \$35,286.22 for the three-year, three-month period reviewed.
- During our examination of the carbon copies of the checks, we found two checks written by the custodian totaling \$304.60 that were not recorded on the custodian's record of CAD expenses for 2007, even though we observed that the memo portion of each check copy identified the check purpose as a CAD expense. Also, two other checks totaling \$180.00 were listed as 2007 CAD expenses on the custodian's records, but a review of the memo portion of each check copy and discussions with the fund custodian and the coordinator of the CAD revealed that the expenses were actually related to the commission's annual fall retreat. The custodian made revisions to the ending balance on the CAD records based on our discussions with him during the review. We believe paying expenses for the commission's fall retreat was an improper use of both the employees' contributions and the CAD sponsorship fees. Any expenses incurred for the commission's fall retreat should have been processed through F&A's Division of Accounts.
- The Executive Director did not ensure that a former employee was removed as an authorized check signer on the TCCY Sunshine Fund bank account when the employee transferred to another state agency on January 1, 2003. The terminated employee was still listed on the account as an authorized signer on April 9, 2008, as confirmed by the financial institution. The Executive Director stated she did not know who the authorized check signers were on the account.
- The fund custodian did not adequately protect unused checks which were stored in an unlocked drawer in his office. We accounted for every check from January 1, 2005, through March 31, 2008.
- The Executive Director did not ensure proper procedures were in place to safeguard incoming checks. Specifically, the secretary did not prepare a log of incoming checks until December 2005 when she decided on her own to begin preparing an unofficial check log when opening the mail. The secretary stated that she began preparing the log for her own benefit when someone called looking for a check. However, the log was not reconciled to the custodian's records or the bank statements. In addition, incoming checks were not stamped "For Deposit Only." On advice from F&A, the commission obtained a "For Deposit Only" stamp and began endorsing incoming

checks in February 2008. Also, the secretary occasionally left unstamped, unsecured checks in the sponsor liaison's mail file when he was out of the office. Improper safeguarding of checks increases the risk of fraud and misappropriation of funds.

Purchasing Guidelines

The Executive Director circumvented state bidding requirements by using the Sunshine Fund account to pay CAD expenses. The Executive Director stated that by not using the State of Tennessee Accounting and Reporting System (STARS) and the state purchasing guidelines, she was better able to maintain control over the quality of the food and services provided for the annual event and purchase wine for the legislative reception portion of the event.

F&A Policy 25

The fund custodian did not deposit funds timely. F&A Policy 25, *Deposit Practices*, states that funds should be deposited immediately and defines immediately as within 24 hours if \$500 has been accumulated, within five working days if more than \$100 but less than \$500 has been accumulated, or at least once per month if \$100 or less has accumulated and is secured under lock and key. Based on review of bank statements and the unofficial check logs maintained by the secretary as noted above, checks received during 2006 and 2007 for CAD were not deposited immediately as defined in F&A Policy 25. For example, a check was received on February 23, 2006, for \$1,000.00 according to the unofficial check log, but the first deposit in 2006 per our review of the bank statements was not until March 15, 2006, which was 15 working days after receipt. The risk of fraud or abuse is greatly increased when checks are not deposited immediately.

Our review of the activity in the account did not disclose any evidence of fraud or abuse; however, we cannot be certain that fraud or abuse did not occur. The Executive Director's failure to establish controls over the account activity, account reconciliations, and account disbursements increases the risk that fraud or abuse could occur and not be detected. The Executive Director's intentional circumvention of STARS and state purchasing guidelines also increases the risk that fraud or abuse could occur and not be detected, and negatively impacts the control environment.

Recommendation

The Executive Director should ensure that all transactions, including all receipts and disbursements related to the CAD, or any other state activities, are processed and accounted for using the appropriate state systems and established procedures. All CAD funds remaining in the Sunshine Fund account should be deposited into an official state bank account.

The Executive Director 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 adequately mitigate those assessed risks and to ensure compliance with applicable requirements.

Management 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 Tennessee Commission on Children and Youth (TCCY) did not know we needed to consider private dollars contributed to support Children's Advocacy Days (CAD) and placed in this account as state dollars. When it came to the attention of the Commission in 2007 that private contributions should be considered state dollars, we began to take steps to treat these private contributions as state dollars. In 2008 around the time the audit began, steps were put in place and all new sponsorship funds were treated as state dollars and deposited in the state's account. As noted in the audit, all except two expenses for CAD in 2008 were paid through the state process. Those two were paid with the remaining private sponsorship funds in the account. In 2009, all sponsorship funds for Children's Advocacy Days were deposited in the state's account and all expenses except some refreshments for the reception were paid through the regular state purchasing process. Sponsorship funds remaining in the account were used for this expenditure.

The audit did not identify any fraud or abuse in this account, only the potential for such. This unauthorized account was opened by the executive director in order to provide a no cost checking account for Commission staff's "sunshine fund" for employee illnesses, losses, or special events. It was not considered a "personal" account and never used for any personal reasons or expenditures. Private CAD sponsorship funds were also processed through this account until the Commission became aware this was not acceptable. Even though the executive director was an authorized signatory on the account, she was never involved in any way with the account. As a result of the audit, it is recognized attention should have been paid to the account.

Near the end of fieldwork of the audit, the executive director had the name on the account changed to eliminate "TCCY" from the name on the account and personally paid for new checks that say only "Sunshine Fund" and also personally paid for all front and back copies of canceled checks requested in the audit process. Commission staff continues to use the "Sunshine Fund" for non-state purposes. The remaining sponsorship funding will be expended supporting Children's Advocacy Days expenditures for some refreshments for the reception in the next year or so.

Once the Commission became aware this would be considered an unauthorized account and not be a permissible way to handle funding for special events, steps were taken to correct the issue. There is no longer a "TCCY Sunshine Fund" account. All Children's Advocacy Days cash sponsorships were processed through the state system for 2008 and 2009 and will be in the future.

TRAVEL EXPENDITURES

Our objectives for reviewing controls and procedures over travel expenditures were to determine whether payments for travel were properly approved and made in accordance with the Comprehensive Travel Regulations.

We tested a nonstatistical sample of travel expenditures from June 1, 2005, through November 30, 2007. Based on our testwork, we determined that payments for travel were properly approved, with minor exceptions, and were made in accordance with the Comprehensive Travel Regulations.

GRANTS AND CONTRACTS

Our objectives for reviewing controls and procedures over grants and contracts were to determine whether

- grant contracts were properly approved;
- payments on grant contracts were made before the contracts were approved;
- grant expenditures were made in accordance with established policies and procedures, were adequately supported, and were properly approved;
- monitoring activities for juvenile detention facilities and county jails complied with the Juvenile Justice and Delinquency Prevention Act guidelines;
- the commission filed annual monitoring plans as required by the Department of Finance and Administration's (F&A) Policy 22, *Subrecipient Contract Monitoring*; and
- the commission monitored grant contracts in accordance with its monitoring plans and F&A Policy 22.

We tested a nonstatistical sample of grant contracts in effect during the period July 1, 2005, through November 20, 2007. We obtained the contracts for each sample item and reviewed the approval signatures. Also, for each contract, we compared the date of the last approval to the first contract payment date to determine whether contract payments were made before the contracts were approved. As a result of testwork performed, we determined that grant contracts were properly approved and that payments were appropriately not made before the grant contracts were approved.

We tested a nonstatistical sample of grant expenditures for the period June 1, 2005, through November 30, 2007. We examined the supporting documentation for each sample transaction including invoices for reimbursement, vendor invoices, and travel claims. As a result

of testwork performed, we determined that grant expenditures were made in accordance with established policies and procedures, were adequately supported, and were properly approved.

We tested a nonstatistical sample from all juvenile detention facilities monitored for fiscal years 2005, 2006, and 2007 for compliance with the Juvenile Justice and Delinquency Prevention (JJDP) Act guidelines. We also tested a nonstatistical sample of the county jail monitoring reports for fiscal years 2005, 2006, and 2007 for compliance with JJDP guidelines. As a result of testwork performed, we determined that the monitoring activities for the juvenile detention facilities and county jails complied with the JJDP guidelines.

We obtained and reviewed the commission's monitoring plans for 2006, 2007, and 2008. As a result of our review, we determined that the commission did file annual monitoring plans as required by F&A Policy 22.

We interviewed key commission management to obtain an understanding of the commission's administrative controls and procedures over monitoring activities. We selected the entire population of high-risk federal grants identified in the commission's 2007 monitoring plan to test for compliance with the plan and F&A Policy 22. Based on the discussions with management and testwork performed, we determined that the commission had not monitored subrecipient contracts in accordance with the commission's monitoring plan and F&A Policy 22. See finding 2.

2. The commission failed to implement adequate controls over monitoring of grant contracts, increasing the risk that noncompliance with contract provisions could occur and not be detected

Finding

As stated in the prior audit, the controls over monitoring of the grant contracts awarded by the commission to local governments and other agencies were not adequate to ensure compliance with state and federal monitoring guidelines. Management concurred with the prior audit finding and summarized a number of steps to improve controls over the monitoring of grant contracts. However, the commission still failed to implement adequate controls over monitoring of grant contracts.

The Department of Finance and Administration's (F&A) Policy 22, *Subrecipient Contract Monitoring*, establishes subrecipient contract monitoring requirements for the State of Tennessee. The policy requires the monitoring of contracts awarded to subrecipients that include state and/or federal funds from state departments, agencies, or commissions. Additionally, the Office of Management and Budget Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*, requires the state to monitor activities of subrecipients and to ensure compliance with program and administrative requirements.

The commission's 2007 monitoring plan indicated that the commission had awarded 147 grant contracts totaling \$3,431,154. The plan identified 65 of these grants totaling \$2,289,327 to be monitored. Fourteen of the 65 grants were identified as high-risk; therefore, we decided to review the monitoring reports and supporting working papers for these 14 grants. Staff provided us with monitoring reports for 5 of the 14 high-risk grants. However, staff could not provide any working papers to support these five monitoring reviews. Furthermore, the monitoring reports were not signed; there was no indication of who performed the monitoring review; there was no evidence that the reports had been reviewed by management; and there was no evidence that the reports had been sent to the subrecipients. In addition, no monitoring was performed for the remaining nine high-risk grants.

We reviewed management's risk assessment to determine if the commission had identified and included the lack of monitoring as a risk. Management had included the risk of subrecipients not being monitored in accordance with the requirements of F&A Policy 22 as a risk; however, management indicated in the assessment that the controls were operating effectively when they were not.

Inadequate monitoring can lead to inappropriate expenditures, noncompliance with contract provisions, and unmet program objectives.

Recommendation

The Executive Director should identify specific staff to be responsible for the design and implementation of internal controls to comply with the monitoring plan and F&A Policy 22. The Executive Director should also identify staff to be responsible for ongoing monitoring for compliance with all requirements and taking prompt action should exceptions occur. The Executive Director should ensure that the commission's risk assessment accurately reflects whether controls are operating effectively.

Management's Comment

We concur.

The Commission did not adequately monitor grantees in 2007. Following the loss of federal funding to support staff dedicated to monitoring, the agency did not get an effective alternative strategy for monitoring implemented until 2008. In 2008, we monitored all required grantees except one and the monitoring plan for 2009 is well under way in implementation.

Management indicated controls were operating effectively in the management risk assessment document completed in late 2007 because the document was accurately forecasting controls for 2008, rather than reflecting on the monitoring inadequacies experienced in 2007.

The Commission's large number of relatively small grants and contracts presents special challenges for Policy 22 compliance, but the agency has procedures in place and has fully complied for 2008, will for 2009, and is committed to continuing compliance. TCCY has designated all federal grants as "high-risk" because they are scheduled to be monitored each year in order to comply with Policy 22 monitoring requirements. In reality few TCCY grants are high-risk, and if they were in other agencies with more funding in grants and contracts, they would not have been identified as high-risk. The 2009 distribution of TCCY grants is typical of other years. Of the 228 grants listed in the Commission's FY09 Policy 22 monitoring plan approved by the Department of Finance and Administration, 73 percent (166) are \$10,000 or less, with 21 percent of all grants (48) less than \$1,000. Only 3 percent of grants (6) are more than \$75,000; 15 percent (35) are between \$10,001 and \$30,000; 10 percent (22) are between \$30,001 and \$75,000. In a large agency, only the six largest grants would be likely to be considered high-risk. Additionally, 83 percent of all grants are to state or local government agencies or universities. In order to meet the Policy 22 requirement to monitor one-third of the grants and two-thirds of the funding annually, substantial TCCY staff time is expended monitoring an inordinate number of small grants.

The Commission is committed to maintaining full compliance with Policy 22 requirements for grant monitoring, as it has in 2008 and 2009, including monitoring small grants.

PAYMENT CARDS

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

- payment card purchases were adequately supported and recorded on the transaction logs;
- payment card purchases were reasonable and necessary for conducting state business;
- payment card purchases had exceeded the single-purchase dollar limit;
- payment card purchases complied with the Department of General Services' *Agency Purchasing Procedures Manual*;
- cardholders' transaction logs were properly approved; and
- cardholders' transaction logs were reconciled to the payment card statements.

We tested a nonstatistical sample of payment card transactions from April 1, 2007, through January 15, 2008. We determined that payment card purchases were adequately supported, were recorded on the transaction logs, were reasonable and necessary for conducting state business, had not exceeded the single-purchase dollar limit, and complied with the *Agency Purchasing Procedures Manual*. We also tested the cardholders' transaction logs related to the

items in the sample. We determined that the cardholders' transaction logs were properly approved and were reconciled to the payment card statements.

FINANCIAL INTEGRITY ACT

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

Our objectives were to determine whether

- the commission's June 30, 2007; June 30, 2006; and June 30, 2005, responsibility letters and December 31, 2007, internal accounting and administrative control report were filed in compliance with Section 9-18-104, *Tennessee Code Annotated*;
- documentation to support the commission's evaluation of its internal accounting and administrative control was properly maintained;
- procedures used in compiling information for the internal accounting and administrative control report were in accordance with the guidelines prescribed under Section 9-18-103, *Tennessee Code Annotated*; and
- corrective actions have been implemented for weaknesses identified in the report.

We reviewed the June 30, 2007; June 30, 2006; and June 30, 2005, responsibility letters and the December 31, 2007, internal accounting and administrative control report to determine whether they had been properly submitted to the Comptroller of the Treasury and the Department of Finance and Administration. We also reviewed the supporting documentation for the commission's evaluation of its internal accounting and administrative control.

We determined that the Financial Integrity Act responsibility letters and internal accounting and administrative control report were submitted on time, support for the internal accounting and administrative control report was properly maintained, and procedures used were in accordance with *Tennessee Code Annotated*. No weaknesses were identified in the report.

OBSERVATIONS AND COMMENTS

REGIONAL COUNCIL BANK ACCOUNTS

Section 37-3-106, *Tennessee Code Annotated*, required the Tennessee Commission on Children and Youth to organize a regional council on children and youth in each of the nine development districts of the state. These nine regional councils are the ongoing communication links between the commission and the various regional and local areas of the state. The councils perform information-gathering and problem-solving tasks concerning services for children and youth. The councils are comprised of voluntary members from each respective region, and council membership ranges from 135 to 250 members per council depending on the region. Each council has an executive board that governs the council.

Section 37-3-106(c), *Tennessee Code Annotated*, requires the commission to provide each regional council with at least one locally based staff person to assist the council in performing its duties. The commission has placed a regional coordinator, who is a state employee, in each of the nine development districts. The regional coordinators are to coordinate, advise, and consult with the council; provide technical assistance to the council and community organizations serving children and youth; and act as liaisons to the commission.

Each regional council maintains a bank account. In the prior audit, we discovered that the regional coordinator in each council had access to the funds for council activities.

The sources of funds for these accounts are primarily membership dues from council members. Other sources include fees from workshops, sponsorships, and donations. The funds from these bank accounts are primarily used for purchases related to council meetings and related council activities, such as workshops, room rentals, refreshments for meetings, trainers, speaker gifts, and donations to the community.

The regional coordinators are involved in the day-to-day operations of the councils. The regional coordinators also have other job duties assigned by the commission including monitoring of secure juvenile facilities and county jails in support of the Juvenile Justice and Delinquency Prevention Act.

In the prior audit, we noted that there were certain circumstances in the structure and operation of the regional council bank accounts that raised questions about their connection with state government. The known factors suggested that the accounts were not totally independent of the state and the commission.

Commission personnel developed guidelines for the administration of the regional council funds, and the guidelines were approved at the full commission meeting in February 2008. These guidelines emphasize transparency and that the collection and disbursement of

money by a regional council—and any liability associated with this activity—shall be the sole responsibility of the members of the regional council.

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.

AUDIT COMMITTEE

On May 19, 2005, the Tennessee General Assembly 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. Entities, pursuant to the act, are required to appoint the audit committee and develop an audit committee charter in accordance with the legislation. The ongoing responsibilities of an audit committee include, but are not limited to:

1. overseeing the financial reporting and related disclosures, especially when financial statements are issued;
2. evaluating management's assessment of risk and the agency's system of internal controls;
3. formally reiterating, on a regular basis, to the board, agency management, and staff their responsibility for preventing, detecting, and reporting fraud, waste, and abuse;
4. serving as a facilitator of any audits or investigations of the agency, including advising auditors and investigators of any information it may receive pertinent to audit or investigative matters;
5. informing the Comptroller of the Treasury of the results of assessment and controls to reduce the risk of fraud; and
6. promptly notifying the Comptroller of the Treasury of any indications of fraud.

In a previous audit report, we recommended that the Tennessee Commission on Children and Youth establish an audit committee. The board of the Tennessee Commission on Children and Youth appointed a four-member audit committee on May 4, 2007. The audit committee charter was approved by the Comptroller of the Treasury on June 12, 2007.

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 Tennessee Commission on Children and Youth filed its compliance reports and implementation plans on May 24, 2007; June 15, 2006; and June 29, 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. 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.