



**STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY**



DEPARTMENT OF FINANCIAL INSTITUTIONS

Financial and Compliance Audit Report

For the Period January 1, 2013, Through December 31, 2014

Justin P. Wilson, Comptroller



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November 30, 2015

The Honorable Bill Haslam, Governor
Members of the General Assembly
The Honorable Greg Gonzales, Commissioner
Department of Financial Institutions

Ladies and Gentlemen:

Transmitted herewith is the audit of the Department of Financial Institutions for the period January 1, 2013, through December 31, 2014.

The review of internal control and compliance with laws, regulations, and provisions of contracts or grant agreements resulted in the finding that is detailed in the Objectives, Methodologies, and Conclusions section of this report.

Sincerely,

A handwritten signature in black ink that reads "Deborah V. Loveless".

Deborah V. Loveless, CPA
Director

15/054

Audit Report
Department of Financial Institutions
For the Period January 1, 2013, Through December 31, 2014

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State of Tennessee

Audit Highlights

Comptroller of the Treasury

Division of State Audit

Financial and Compliance Audit Department of Financial Institutions For the Period January 1, 2013, Through December 31, 2014

Audit Scope

We have audited the Department of Financial Institutions for the period January 1, 2013, through December 31, 2014. Our audit scope included a review of internal control and compliance in the areas of examinations of financial institutions; payment cards; travel; payroll and personnel; revenue; and equipment. The audit was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States.

Audit Finding

Management did not establish adequate controls in one specific area

There were internal control deficiencies in one specific area. The details of this finding are confidential pursuant to Section 10-7-504(i), *Tennessee Code Annotated* (page 7).

Audit Report
Department of Financial Institutions
For the Period January 1, 2013, Through December 31, 2014

INTRODUCTION

Post-Audit Authority

This audit of the Department of Financial Institutions was conducted pursuant to Section 8-4-109, *Tennessee Code Annotated*, which 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 Financial Institutions provides the citizens of Tennessee a supervised and sound system of state-chartered and state-licensed financial institutions. These include commercial banks; trust companies; savings institutions; credit unions; industrial loan and thrift companies; business and industrial development corporations; deferred presentment and check cashing companies; mortgage lenders, brokers, servicers, and originators; insurance premium finance companies; flexible credit act lenders; and money transmitters.

The department's primary statutory mission is to provide the people of Tennessee with a safe and sound system of banks and other institutions; to ensure safety, soundness, and compliance with governing law; and to give institutions the opportunity to contribute to the economic progress of Tennessee and the nation.

The department has 163 authorized positions for fiscal year 2015 and a budget of approximately \$19,969,100.

AUDIT SCOPE

We have audited the Department of Financial Institutions for the period January 1, 2013, through December 31, 2014. Our audit scope included a review of internal control and compliance with laws and regulations in the areas of examinations of financial institutions; payment cards; travel; payroll and personnel; revenue; and equipment. The audit was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We

believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

PRIOR AUDIT FINDING

Section 8-4-109, *Tennessee Code Annotated*, requires that each state department, agency, or institution report to the Comptroller of the Treasury the action taken to implement the recommendations in the prior audit report. The Department of Financial Institutions filed its report with the Department of Audit on July 31, 2009. A follow-up of the prior audit finding was conducted as part of the current audit.

The current audit disclosed that the Department of Financial Institutions has corrected a previous audit finding concerning the following:

- computer security access policy,
- computer security request form,
- separation checklist, and
- unique user names.

OBJECTIVES, METHODOLOGIES, AND CONCLUSIONS

Examinations of Financial Institutions

The objectives of our review of the controls and procedures over the examinations of financial institutions were to determine

- whether the frequency of examinations of banks, credit unions, and non-depository financial institutions was in compliance with applicable laws and regulations and
- whether non-depository financial institutions' most recent licenses were properly approved.

We interviewed key personnel and reviewed supporting documentation to gain an understanding of the department's procedures and controls over the bank division. We tested a nonstatistical¹ sample of 25 of 159 banking institutions for the period of January 1, 2013, through December 31, 2014, to determine whether the frequency of examinations was in compliance with applicable laws and regulations.

Based on our interviews, review of supporting documentation, and testwork performed, we determined that the frequency of examinations was in compliance with applicable laws and regulations.

We interviewed key personnel and reviewed supporting documentation to gain an understanding of the department's procedures and controls over the credit union division. We tested a nonstatistical¹ sample of 25 of 102 credit unions for the period of January 1, 2013, through December 31, 2014, to determine whether the frequency of examinations was in compliance with applicable laws and regulations.

Based on our interviews, review of supporting documentation, and testwork performed, we determined that the frequency of examinations was in compliance with applicable laws and regulations.

We interviewed key personnel and reviewed supporting documentation to gain an understanding of the controls and procedures over the compliance division. We tested a nonstatistical¹ sample of 26 of 15,398 non-depository financial institutions regulated by the department for the period of January 1, 2013, through December 31, 2014, to determine whether the frequency of the department's examinations was in compliance with applicable laws and regulations and whether evidence existed that appropriate department personnel had approved the licenses of non-depository financial institutions.

Based on our reviews, interviews, and testwork performed, we determined the frequency of the department's examinations was in accordance with applicable laws and regulations, and that licenses for non-depository financial institutions were properly approved.

Payment Cards

The objectives of our review of the payment card controls and procedures were to determine whether

- payment card holders had credit card agreements;
- purchases did not appear to have been split into multiple items to avoid bid requirements;
- no Tennessee state sales tax was charged;
- purchases were not for items prohibited by Department of Finance and Administration's State Payment Card policy;
- procurement card holders did not exceed the assigned single-purchase limit;
- purchases were adequately supported with documentation and agreed to amounts recorded in the transaction log;
- purchased items were not covered by a statewide contract; and

- purchases appeared reasonable and necessary for conducting state business.

We interviewed key personnel and reviewed supporting documentation to gain an understanding of the controls and procedures over payment cards. We reviewed the cardholder agreements for the two cardholders to determine if they were valid cardholders. We tested a nonstatistical¹ sample of payment card purchases totaling \$4,205.18 from a population of \$145,598.19 for the period January 1, 2013, through December 31, 2014, for adequate documentation and compliance with Finance and Administration's State Payment Card policy requirements listed above.

Based on our interviews, review of supporting documentation, and testwork performed, we determined that cardholders had valid card agreements, and purchases were in compliance with Finance and Administration's State Payment Card policy requirements listed above.

Travel

The objective of our review of the travel controls and procedures was to determine whether

- payments for travel were made in accordance with the Comprehensive Travel Regulations issued by the Department of Finance and Administration.

We interviewed key personnel and reviewed supporting documentation to gain an understanding of the department's procedures and controls over travel. We also tested a nonstatistical¹ sample of 25 travel claims paid, totaling \$10,889.09, from a population of \$914,407.47 during the period January 1, 2013, through December 31, 2014, to determine whether travel claims were adequately supported and complied with regulations.

Based on our reviews, interviews, and testwork performed, we determined that payments for travel were made in accordance with the Comprehensive Travel Regulations.

Payroll and Personnel

The objectives of our review of the payroll and personnel controls and procedures of the Department of Financial Institutions were to determine whether

- the initial wage was correct for newly hired employees;
- documentation indicated that newly hired employees were qualified for their positions;
- terminated employees' final pay was accurate;
- appropriate controls had been established in specific areas;
- current employees' access to department-specific systems and applications was accurately documented and approved; and

- payroll disbursements were made for work performed by employees of the department.

We interviewed key personnel and reviewed supporting documentation to gain an understanding of the department's procedures and controls over payroll and personnel. We tested a nonstatistical¹ sample of 25 employees from a population of 64 new hires and terminated employees for the period January 1, 2013, through December 31, 2014, to determine whether the salary in Edison for the new hires agreed to the salaries recorded in their personnel files. For newly hired employees, we reviewed personnel files to determine if they contained documentation indicating the employees possessed the qualifications for their job.

For terminated employees, we compared information in their personnel files to leave balances in Edison at the time of the termination to determine the accuracy of the employees' annual leave balances. Also for terminated employees, we reviewed dates the department notified Finance and Administration of the employees' terminations to determine if such notifications were timely.

We reviewed specific controls for adequacy.

We tested the access to department-specific systems for a nonstatistical¹ sample of 25 from a population of 148 current employees to determine whether their security access documentation was approved by appropriate personnel and whether the employees had access that was not indicated in the documentation.

To determine whether payroll disbursements were made for work performed by employees of the department, we selected a nonstatistical¹ sample of 25 employees from a list of 148 employees at December 31, 2014. We verified their employment in person or by phone.

Based on interviews, review of supporting documentation, and testwork performed, we determined that

- the initial wage was correct for newly hired employees;
- documentation indicated that newly hired employees were qualified for their positions;
- terminated employees' final pay was accurate;
- as stated in the finding below, management did not establish adequate controls in one specific area;
- current employees' access to department-specific systems and applications was accurately documented and approved; and
- payroll disbursements were made for work performed by employees of the department.

Management did not establish adequate controls in one specific area

Finding

There were internal control deficiencies in one specific area. Management did not establish internal controls as required by state policies or industry best practices. The details of this finding are confidential pursuant to Section 10-7-504(i), *Tennessee Code Annotated*. We provided the department with detailed information regarding the specific conditions we identified, as well as our recommendations for improvement.

Recommendation

The Commissioner should ensure that these conditions are remedied by the prompt development and implementation of effective controls. In addition, the Commissioner should ensure that the risks associated with this finding are adequately identified and assessed in the department's documented risk assessment. The Commissioner should implement effective controls to ensure compliance with applicable requirements; assign staff to be responsible for the ongoing monitoring of the risks and mitigating controls; and take action if deficiencies occur.

Management's Comment

We concur. The department takes our internal controls very seriously. Immediately upon notice from the audit team of internal control deficiencies (during the course of the audit) the department began to take steps to develop effective controls. In fact, the department drafted an internal policy to address the internal control deficiencies prior to the audit team leaving the department. The policy was dated September 3, 2015. This policy assigns staff to be responsible for the ongoing monitoring of the risks and mitigating controls and also includes our internal auditor in the oversight of compliance with the internal policy. The department has also taken steps to document that these risks and controls are identified in the department's risk assessment.

Revenue

The objectives of our review of the controls and procedures over revenue were to determine whether

- cash receipts for the compliance division were correctly recorded and supported;
- cash receipts for the compliance division were deposited in accordance with Department of Finance and Administration policy; and
- cash receipts for the compliance division were reconciled with recorded revenues.

We interviewed key personnel and reviewed supporting documentation to gain an understanding of the department's procedures and controls over revenues. We tested a nonstatistical¹ sample of cash receipt transactions for 26 of 15,398 non-depository financial institutions regulated by the department for the period of January 1, 2013, through December 31, 2014, to determine if cash receipts were correctly recorded and supported, were deposited within one business day, and were reconciled with reported revenue.

Based on our interviews, review of supporting documentation, and testwork performed, we determined that cash receipts for the compliance division were correctly recorded and supported, deposited in compliance with the Department of Finance and Administration policy, and reconciled with recorded revenue.

Equipment

The objectives of our review of the controls and procedures over equipment were to determine whether

- a physical inventory was completed during the audit period;
- lost or stolen equipment was properly reported to the Comptroller's Office as required by Section 8-19-501, *Tennessee Code Annotated*; and
- equipment items selected from the department's inventory listing could be located.

We interviewed key personnel and reviewed supporting documentation to gain an understanding of the department's controls and procedures over equipment. We tested a nonstatistical¹ sample of 25 equipment items from the population of 424 items to determine whether equipment could be located and whether the tag numbers, serial numbers, and the equipment type agreed to the inventory listing.

Based on the interviews, review of supporting documentation, and testwork performed, we determined that a physical inventory was completed during the review period, lost or stolen equipment was properly reported, and equipment items selected from the department's inventory listing could be located.

¹ For our sample design, we used nonstatistical audit sampling, which was the most appropriate and cost-effective method for concluding on our audit objectives. Based on our professional judgment, review of authoritative sampling guidance, and careful consideration of underlying statistical concepts, we believe that nonstatistical sampling provides sufficient appropriate audit evidence to support the conclusions in our report. This sample was selected in such a manner as to permit the results to be projected to the population from which the sample was drawn.