

**Department of Employment Security**

**For the Year Ended  
June 30, 1999**

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STATE OF TENNESSEE  
**COMPTROLLER OF THE TREASURY**

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John G. Morgan  
Comptroller

May 26, 2000

The Honorable Don Sundquist, Governor  
and  
Members of the General Assembly  
State Capitol  
Nashville, Tennessee 37243  
and

The Honorable Michael E. Magill, Commissioner  
Department of Employment Security  
Second Floor, Andrew Johnson Tower  
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have conducted a financial and compliance audit of selected programs and activities of the Department of Employment Security for the year ended June 30, 1999.

We conducted our audit in accordance with generally accepted auditing standards and the standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. These standards require that we obtain an understanding of management controls relevant to the audit and that we design the audit to provide reasonable assurance of the department's compliance with the provisions of laws, regulations, contracts, and grants significant to the audit. Management of the Department of Employment Security is responsible for establishing and maintaining internal control and for complying with applicable laws and regulations.

Our audit disclosed certain findings which are detailed in the Objectives, Methodologies, and Conclusions section of this report. The department's administration 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/or instances of noncompliance to the Department of Employment Security's management in a separate letter.

Sincerely,

John G. Morgan  
Comptroller of the Treasury

JGM/  
99/089

State of Tennessee

# Audit Highlights

Comptroller of the Treasury

Division of State Audit

Financial and Compliance Audit  
**Department of Employment Security**  
For the Year Ended June 30, 1999

## AUDIT SCOPE

We have audited the Department of Employment Security for the period July 1, 1998, through June 30, 1999. Our audit scope included those areas material to the Tennessee Comprehensive Annual Financial Report for the year ended June 30, 1999, and the Tennessee Single Audit Report for the same period. In addition to those areas, our primary focus was on management's controls and compliance with policies, procedures, laws, and regulations in the areas of payroll, interstate benefits receivable, employer tax receivable, benefit overpayment receivable, revenue, unemployment tax, unemployment benefits, field office visits, utilization of the Department of Finance and Administration's STARS grant module to record the receipt and expenditure of federal funds, detection of unauthorized claims—special investigation and unauthorized use of state resources—special investigation. The audit was conducted in accordance with generally accepted auditing standards and the standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

## AUDIT FINDINGS

### **The Department Did Not Effectively Review the Allowability of Costs Charged to the Trade Adjustment Assistance Program**

Invoices, receipts, and other documentation supplied by vendors in requests for reimbursements of Trade Adjustment Assistance (TAA) training costs were not reviewed to ensure reasonableness, necessity, and adequate documentation (page 4).

### **SPECIAL INVESTIGATIONS**

#### **Improper Authorization of Benefits and Solicitation of a Kickback**

The department did not have a systematic process to promptly review claims that were denied and later improperly approved and paid (page 14).

#### **Weaknesses in Supervision and Monitoring Enabled a Department Manager to Abuse His Position**

A Nashville Special Projects Office manager used state office space, time, and resources for unauthorized purposes (page 17).

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“Audit Highlights” is a summary of the audit report. To obtain the complete audit report which contains all findings, recommendations, and management comments, please contact

Comptroller of the Treasury, Division of State Audit  
1500 James K. Polk Building, Nashville, TN 37243-0264  
(615) 741-3697

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**Audit Report**  
**Department of Employment Security**  
**For the Year Ended June 30, 1999**

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# Department of Employment Security For the Year Ended June 30, 1999

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

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

### BACKGROUND

The mission of the Department of Employment Security is to enhance the quality of life in Tennessee by providing responsive job referrals to employers; productive client counseling services; an impartially administered, sound, and competitive unemployment insurance program; and reliable and relevant data to foster job development for Tennesseans.

In order to fulfill this mission, the department has four primary sections: Unemployment Insurance, Employment Service, Administration, and Field Operations.

Unemployment Insurance is a joint federal and state program that provides benefits to unemployed workers who lose their jobs through no fault of their own. Unemployment Insurance benefits are paid from the Tennessee Unemployment Insurance Trust Fund. This fund is used only to pay benefits to Tennessee’s unemployed, and the fund is financed entirely by Tennessee employers.

Employment Services provides counseling, training, and job development services to applicants to enhance their employability. Employment Service also provides employers services such as job listings over the phone, pre-screening of applicants, pre-testing of clerical personnel, aptitude testing, on-site screening, and computerized job listings.

The department is also responsible for compiling Tennessee employment data. Information provided includes employment and unemployment data by county; jobs by industry; wages of

selected occupations for various regions of the state; future trends in occupations and industries; population and demographic data; per capita income data; and affirmative action data.

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

Effective July 1, 1999, the Department of Employment Security was combined with the Department of Labor to form the Department of Labor and Workforce Development.

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## AUDIT SCOPE

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We have audited the Department of Employment Security for the period July 1, 1998, through June 30, 1999. Our audit scope included those areas material to the Tennessee Comprehensive Annual Financial Report for the year ended June 30, 1998, and to the Tennessee Single Audit Report for the same period. In addition to those areas, our primary focus was on management's controls and compliance with policies, procedures, laws, and regulations in the areas of payroll, interstate benefits receivable, employer tax receivable, benefit overpayment receivables, revenue, unemployment tax, unemployment benefits, field office visits, utilization of the Department of Finance and Administration's STARS grant module to record the receipt and expenditure of federal funds, detection of unauthorized claims—special investigation and unauthorized use of state resources—special investigation. The audit was conducted in accordance with generally accepted auditing standards and the standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

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## OBJECTIVES, METHODOLOGIES, AND CONCLUSIONS

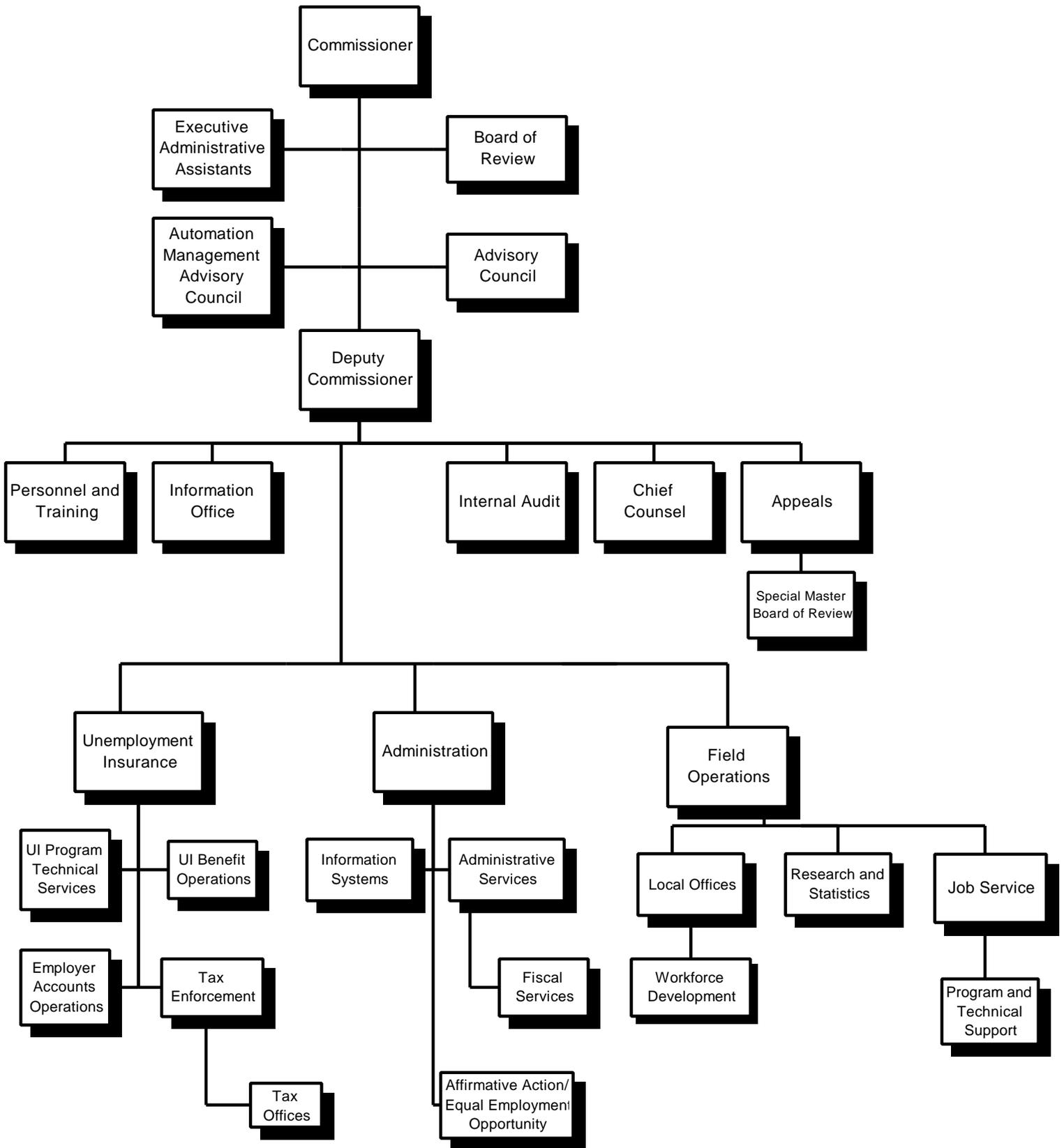
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### AREAS RELATED TO TENNESSEE'S COMPREHENSIVE ANNUAL FINANCIAL REPORT AND SINGLE AUDIT REPORT

Our audit of the Department of Employment Security is an integral part of our annual audit of the Comprehensive Annual Financial Report (CAFR). The objective of the audit of the CAFR is to render an opinion on the State of Tennessee's general-purpose financial statements. As part of our audit of the CAFR, we are required to gain an understanding of the state's internal control and determine whether the state complied with laws and regulations that have a material effect on the state's general-purpose financial statements.

Our audit of the Department of Employment Security is also an integral part of the Tennessee Single Audit, which is conducted in accordance with the Single Audit Act, as amended by the Single Audit Act Amendments of 1996. The Single Audit Act, as amended, requires us to determine whether

# Department of Employment Security Organization Chart



- the state complied with rules and regulations that may have a material effect on each major federal financial assistance program, and
- the state has internal control to provide reasonable assurance that it is managing its major federal award programs in compliance with applicable laws and regulations.

We determined the following areas within the Department of Employment Security were material to the CAFR: the Unemployment Trust Fund, the Employment Service Program, and the Unemployment Insurance Program. We determined that the Employment Service Program, the Unemployment Insurance Program, and the Trade Adjustment Assistance Program were material to the Single Audit Report.

To address the objectives of the audit of the CAFR, as they pertain to the Unemployment Trust Fund, we interviewed key department employees, reviewed applicable policies and procedures, and tested representative samples of transactions, as appropriate. Our testwork on the Unemployment Trust Fund included tests of eligibility of unemployment recipients, tests of the calculation of unemployment taxes paid by employers, tests of receivable balances, confirmation of cash balances and interstate benefits receivable, and other analytical procedures to determine if the financial statements are fairly presented. Our work on the Unemployment Trust Fund was an integral part of the CAFR audit, and the financial statements of the trust and agency funds are presented in the CAFR.

To address the objectives of the audit of the CAFR and the Single Audit Report, as they pertain to the Employment Service Program, the Unemployment Insurance Program, and the Trade Adjustment Assistance Program, we interviewed key department employees, reviewed applicable policies and procedures, and tested representative samples of transactions.

We have audited the general-purpose financial statements of the State of Tennessee for the year ended June 30, 1999, and have issued our report thereon dated December 10, 1999. The opinion on the financial statements is unqualified. The Tennessee Single Audit Report for the year ended June 30, 1999, will include our reports on the schedule of expenditures of federal awards and on internal control and compliance with laws and regulations.

We determined that the department did not effectively monitor the allowability of costs charged to the Trade Adjustment Assistance Program as discussed in finding 1. In addition to the finding, other minor weaknesses came to our attention and have been reported to management in a separate letter.

1. **The department did not effectively review the allowability of costs charged to the Trade Adjustment Assistance Program**

**Finding**

The Department of Employment Security did not adequately review invoices, receipts, and other documentation supplied by vendors in requests for reimbursements of Trade Adjustment

Assistance (TAA) training costs. The TAA Training Coordinator did not review the charges to ensure that they were reasonable, necessary, and adequately documented.

The Trade Adjustment Assistance program was created to provide assistance for individuals who become unemployed due to situations such as increased imports. The TAA program can provide participants with training assistance in the form of payment for educational expenses that will allow the participant to enter a new trade or business. The Trade Act, Part 617.11(a) (6) (iii) (A), states that the costs of a training program shall include tuition and related expenditures such as books, tools, and academic fees.

The department enters into contracts with the program participant and the training institution. The contracts outline the types of training to be provided and the total amounts of assistance. In addition, the contracts between the training institutions and the department contain attachments that provide itemized estimates of educational expenses. These expenses include class fees, textbooks, lab fees, and other necessary supplies and materials. The contracts also state that non-training expenses shall be the responsibility of the participant. The institution is responsible for submitting invoices and approval for payment. However, the coordinator does not adequately review the invoices to ensure that only allowable expenses are paid. The Fiscal Services staff reviews the invoices to determine that the contract amount is not exceeded prior to payment.

Testwork for a sample of 52 expenditures totaling \$17,564.08 revealed the following:

- One of 52 expenditures (2%) tested was not adequately documented. The invoice for \$897.92 did not provide an itemized explanation of the expenses.
- Two of 52 expenditures (4%) tested were not allowable. Items including a cassette tape recorder, cassette tapes, and batteries, totaling \$73.45, were not allowable expenditures under the contract, grant, and/or federal guidelines.

Also, additional testwork revealed that items totaling \$219.01 were not allowable expenditures under the contract, grant, and/or federal guidelines. These items included a graduation pin, graduation pictures, and photocopies.

For the fiscal year ended June 30, 1999, the department reported training expenditures in the amount of \$523,000,000. The total questioned cost was determined to be \$1,190.38. We believe that likely federal questioned cost associated with this condition could exceed \$10,000.00.

Office of Management and Budget Circular A-87(C)(2) provides the following regulations regarding the allowability of charges to federal programs:

A cost is reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the cost. The question of reasonableness is particularly important when governmental units or components are predominately federally

funded. In determining reasonableness of a given cost, consideration shall be given to:

- a) Whether the cost is of a type generally recognized as ordinary and necessary for the operation of the governmental unit or the performance of the Federal award . . .
- d) Whether the individuals concerned acted with prudence in the circumstances considering their responsibilities to the governmental unit, its employees, the public at large, and the Federal Government.
- j) Be adequately documented.

If invoices are not reviewed for allowability prior to payment, then improper charges could have been made to the program and not have been detected. This could also result in a loss of funding for this program.

### **Recommendation**

The TAA Training Coordinator should ensure that charges made against the contracts funded under the TAA program are reviewed for reasonableness, necessity, and adequate documentation prior to payment.

### **Management's Comment**

We concur in part with the finding. Following is our response to the issues raised in the audit report.

Issue 1: One of 52 expenditures (2%) tested was not adequately documented. The invoice for \$897.92 did not provide an itemized explanation of the expenses.

We concur that an itemized receipt should be required for all expenditures. Invoices will be reviewed and all participating training institutions will be reminded of this requirement.

Issue 2: Two of 52 expenditures (4%) tested were not allowable. Items including a cassette tape recorder, cassette tapes, and batteries, totaling \$73.45, were not allowable expenditures under the contract, grant, and/or federal guidelines.

We concur with the findings associated with the purchase of the batteries and the cassette tapes. Although we do not dispute its existence, we were unable to document the purchase of a tape recorder in our review of the designated invoices.

On February 9, 2000, a professor in the Business School at Motlow State Community College was contacted to evaluate the need for a tape recorder in the Business School. Her response follows: "The course work in the Business School is comprehensive and intense. Occasionally, when adults who have been working return to the academic environment, they may not be as skilled at listening and taking notes as their peers. Utilizing a tape recorder can minimize this barrier, allowing time for an adjustment and the opportunity to maintain the demanding pace in the classroom."

We believe that in the interest of promoting successful occupational training that leads to prompt productive re-employment, school aides such as calculators and tape recorders should be evaluated on a case-by-case basis. However, subject equipment will only be purchased with permission from the Regional Office.

Issue 3: Also, additional testwork revealed that items totaling \$219.01 were not allowable expenditures under the contract, grant, and/or federal guidelines. These items included a graduation pin, graduation pictures, and photocopies.

Graduation pins and pictures are listed as a requirement and are approved for purchase by the Regional Office. Students have the option of selecting their pins from three levels of quality. The current prices are \$48.50, \$54.50, and \$103.50. We agree that one of the students selected the most expensive pin.

The Tennessee Department of Labor and Workforce Development will inform the training institutions that, in the future, all costs exceeding the mid-level of quality (\$54.50) will be the responsibility of the participant.

Graduation pictures are also listed as a requirement. Per a discussion on February 7, 2000, with a secretary for the Walter State Division of Health Program, all nursing students are required to provide two photographs. The nursing school maintains one copy for their files. A second copy is required for identification for the state nursing exam. Occasionally, students order additional copies for identification during their hospital rotation.

The amount of \$16.95 for one student's pictures was acceptable. However, \$40.00 and \$30.36, which paid for two sittings for one student, are unacceptable. We agree that one of these photo sessions should not have been paid for with TAA money.

Invoices will be more thoroughly reviewed to avoid unacceptable expenditures. Training institutions will be instructed to tell students that they are limited to two pictures for identification purposes only. Any cost incurred for additional pictures will be each student's responsibility.

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## **PAYROLL**

The objectives of our review of the department's payroll controls and procedures were to determine whether

- payroll (wages, salaries, and benefits) disbursements were made only for work authorized and performed;
- payroll was computed using rates and other factors in accordance with contracts and relevant laws and regulations; and
- payroll and related liabilities were recorded correctly as to amount and period, and distributed properly by account, fund, and budget category.

We interviewed key personnel to gain an understanding of the department's procedures and controls over payroll. We also tested a nonstatistical sample of payroll. We had no findings related to payroll.

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## **INTERSTATE BENEFITS RECEIVABLES**

The objectives of our review of interstate benefits controls and procedures were to determine whether

- revenue amounts uncollected and presented as receivable at the end of the fiscal period were valid; and
- procedures to collect past due accounts were adequate.

We interviewed key personnel to gain an understanding of the department's procedures and controls over interstate benefits. We also tested a nonstatistical sample of interstate benefits. We had no findings related to interstate benefits.

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## **EMPLOYER TAX RECEIVABLES**

The objectives of our review of the controls and procedures for employer tax receivables were to determine whether

- revenue amounts uncollected and presented as receivable at the end of the fiscal period were valid;
- procedures to collect past due accounts were adequate; and
- an adequate allowance for uncollectible accounts had been established.

We interviewed key personnel to gain an understanding of the department's procedures and controls over employer tax receivables. We tested a nonstatistical sample of receivables. We also tested receivables of \$25,000 or greater. We had no findings related to employer tax receivables. Minor weaknesses came to our attention and have been reported to management in a separate letter.

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## **BENEFIT OVERPAYMENT RECEIVABLES**

The objectives of our review of the controls and procedures for benefit overpayment receivables were to determine whether

- revenue amounts uncollected and presented as receivable at the end of the fiscal period were valid;
- procedures to collect past due accounts were adequate; and
- an adequate allowance for uncollectible accounts had been established.

We interviewed key personnel to gain an understanding of the department's procedures and controls over benefit overpayment receivables. We also tested a nonstatistical sample of benefit overpayment receivables. We had no findings related to benefit overpayment receivables.

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## **REVENUE**

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

- revenues that were available and measurable in the fiscal period were recorded;
- revenues or fees were billed or charged and recorded at the correct amount; and
- revenues were properly classified by fund type in the financial statements and related disclosures were adequate.

We interviewed key personnel to gain an understanding of the department's procedures and controls over revenues. We also tested a nonstatistical sample of revenues. We had no findings related to revenue; however, other minor weaknesses came to our attention and have been reported to management in a separate letter.

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## **CONTINGENT AND DEFERRED REVENUE**

The objectives of our review of contingent and deferred revenue controls and procedures were to determine whether

- year-end contingent and deferred revenue accounts per departmental records reconciled with STARS reports;
- earned revenue is transferred from the contingent and deferred revenue accounts in a timely manner; and
- contingent and deferred revenue accounts are used for the proper purpose.

We interviewed key personnel to gain an understanding of the department's procedures and controls over contingent and deferred revenue. We also tested a nonstatistical sample of contingent and deferred revenue. We had no findings related to revenue.

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## **UNEMPLOYMENT TAX**

The objectives of our review of unemployment tax controls and procedures were to determine whether

- the department had complied with applicable provisions of *Tennessee Code Annotated*;
- employer taxes were properly computed and transferred to the trust fund;
- refunds issued to employers were reasonable and adequately supported; and
- penalties and interest were charged when applicable and accounted for properly.

We interviewed key personnel to gain an understanding of the department's procedures and controls over unemployment tax. We also tested nonstatistical samples of taxpayer accounts and refunds to taxpayers. We had no findings related to unemployment tax.

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## **UNEMPLOYMENT BENEFITS**

The objectives of our review of unemployment benefits controls and procedures were to determine whether

- the department had complied with applicable provisions of *Tennessee Code Annotated*;
- benefit amounts were properly computed; and
- only eligible recipients received benefits.

We interviewed key personnel to gain an understanding of the department's procedures and controls over unemployment benefits. We also tested a nonstatistical sample of benefit recipients. We had no findings related to unemployment benefits.

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## **FIELD OFFICE VISITS**

The objectives of our field office visits were to determine whether

- equipment could be physically located;
- leave and attendance were in accordance with state policy;
- payroll costs were allocated properly; and
- proper claim taking procedures for unemployment benefits claimants were followed.

We interviewed key personnel to gain an understanding of the department's procedures and controls over equipment, payroll, and unemployment benefits. We also tested a nonstatistical sample of equipment, payroll, and unemployment benefits. We had no findings related to field office visits; however, other minor weaknesses came to our attention and have been reported to management in a separate letter.

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## **DEPARTMENT OF FINANCE AND ADMINISTRATION POLICY 20, "RECORDING OF FEDERAL GRANT EXPENDITURES AND REVENUES"**

Department of Finance and Administration Policy 20 requires that state departments whose financial records are maintained on the State of Tennessee Accounting and Reporting System (STARS) fully utilize the STARS Grant Module to record the receipt and expenditure of all federal funds. The Department of Employment Security has received an exception to this policy. Because of the unique nature of the department's grants, a cost-accounting system based on time distribution is used. STARS does not have the ability to distribute indirect costs to programs based on the percentage of time charged to each program.

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## **SPECIAL INVESTIGATIONS**

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### **Improper Authorization of Benefits and Solicitation of a Kickback**

On August 19, 1998, staff at Tennessee Department of Employment Security's (TDES) Nashville Metro Local Office received a cassette tape containing a recorded conversation that indicated that a TDES Interviewer II ("the interviewer") may have improperly caused an unqualified claimant to receive unemployment benefits and subsequently solicited a kickback from that ineligible recipient. The tape was forwarded by the TDES local office, through its Division of Field Operations, to TDES Internal Audit for review. The Division of State Audit was notified by TDES Internal Audit on August 26, 1998. A Special Report on the results of the review was released on January 10, 2000.

The objectives of the review were

- to determine whether the interviewer had improperly caused unqualified claimants to receive unemployment benefits;
- to determine whether the interviewer subsequently solicited kickbacks from such ineligible recipients;
- to obtain repayment of misappropriated funds;
- to make recommendations to TDES management on how to avoid similar future losses; and
- to refer the results of the review to the Office of the State Attorney General and, if appropriate, the relevant Office of the District Attorney General.

Division of State Audit staff, in conjunction with TDES internal auditors, reviewed relevant claims records, office sign-in sheets, personnel records, on-line update reports, TDES Voice Response System reports, and provisions of the *Internal Security Handbook (Handbook)* and *Tennessee [Department of] Employment Security Manual (Security Manual)*. Auditors also examined the contents of the interviewer's work area, and conducted interviews with the ineligible recipient who recorded the interviewer's request for a monetary kickback, and with the ineligible recipient's boyfriend, who delivered the recording to TDES. Statements were also taken from three of the interviewer's co-workers as well as from a manager of a private financial services company. The interviewer was given the opportunity to discuss with auditors the evidence gathered against him but declined to address the allegations and opted to consult an attorney.

The review substantiated that the interviewer violated provisions of the *Handbook* in his handling of the claim of the ineligible recipient. The *Handbook* provisions forbid (1) request or acceptance of consideration other than regular pay in return for the performance of official duties; (2) input of false data into TDES records; (3) use of other employees' computer access codes; (4) unauthorized alteration of official documents; (5) unauthorized release of confidential information; and (6) unauthorized personal use of the TDES fax machine. The interviewer's violations caused the ineligible recipient to receive \$1,810 of unemployment benefits she was ineligible to receive.

In addition to the interviewer's primary violation that caused the ineligible receipt of benefits, one instance was found in which the interviewer did not follow procedures, outlined in the *Security Manual*, for releasing claimant information. Contrary to provisions of the *Security Manual*, the interviewer provided a claimant's benefit history to a private financial services company without first obtaining a signed release from the claimant. Release of the information would have been proper had the claimant's signed authorization been first obtained.

The interviewer also sent one fax to, and received two faxes from, a personal friend on April 20, 1998, and April 21, 1998. Those faxes involved long distance telephone calls. The subject matter of the faxes involved a discussion of the tornadoes that occurred in Nashville at that time. The outgoing fax call was in violation of a *Handbook* provision requiring the use of personal billing methods when making long distance personal calls from the office. *Handbook*

provisions do not specifically address the receipt of personal faxes on the machine, but the machine's use of TDES fax paper to reproduce personal faxes would be forbidden under provisions regarding use of state property for personal gain.

Two of the interviewer's co-workers were found to have violated *Handbook* provisions by making it possible for the interviewer to use their access codes to input data into the TDES computer system by failing to properly protect their codes from unauthorized use. Currently available evidence indicates that the interviewer entered a reopening claim on May 13, 1998, using one co-worker's access code, and used another co-worker's access code to enter a reopening claim on August 4, 1998. It is unclear how the interviewer obtained their access codes, but the *Handbook* holds each employee strictly liable for all entries under his or her code and provides specific instructions on how to prevent other persons from obtaining it. The two co-workers each received a written reprimand for violating *Handbook* provisions by making it possible for the interviewer to use their access codes to enter data into the TDES computer system.

On September 30, 1998, the interviewer signed an agreement with TDES that allowed him to resign, in lieu of termination for misconduct, without acknowledging either the nature or content of these charges against him. The terms of that agreement also provided that, in accord and satisfaction of any civil debt or obligations attributable to this matter, TDES would withhold \$1,800 from salary, leave, and bonus amounts due the interviewer. On February 4, 1999, the Office of the District Attorney General, Twentieth Judicial District (Davidson County), was notified of the findings related to the activities of the interviewer, and that office is reviewing the matter.

After the interviewer had left his position with the state, auditors found that he may have caused a second ineligible claimant to receive benefits. During a routine quarterly "cross match," conducted by TDES' Benefit Payment Control unit, the second ineligible recipient was among a list of claimants who had concurrently received benefits as well as wages. The fact that the second ineligible recipient had apparently dealt with the interviewer caused TDES Internal Audit staff to examine her records.

That examination revealed that the second ineligible recipient's claim was similar to that of the first. The approved claim existed as a single computer transaction without any supporting paperwork. Such claims are normally supported by substantial documentation.

During the period from February 1, 1998, through May 25, 1998, the second ineligible recipient received checks, totaling \$3,533, after having had both the claimant's initial application and subsequent appeal denied. On December 15, 1998, TDES Internal Audit staff interviewed the second ineligible recipient, who confirmed that the interviewer in question was the same person who serviced the first ineligible recipient. The internal auditors found that on January 22, 1998, the access code of one of the same co-workers of the interviewer had been used to approve the second ineligible recipient's claim.

Although the interviewer apparently never asked the second ineligible recipient for any money, the interviewer did request a date with the second recipient. The second recipient stated that such a date never took place.

## 2. **Weaknesses in internal controls enabled unauthorized claims to escape detection**

### **Finding**

This review disclosed two internal weaknesses.

- First, two employees failed to comply with policies requiring that they maintain the confidentiality of their computer access passwords.
- Second, the department did not have a systematic process to promptly review claims that were denied and later approved and paid. Such a review should involve the examination of all supporting documentation to determine that the award was appropriate.

### **Recommendation**

Department management should further emphasize its employees' responsibilities regarding the safeguarding of computer passwords.

Department management should ensure that there are periodic reviews of claims initially rejected yet later approved. Such reviews should be documented and maintained.

Field Office supervisors should periodically review documents relating to claims to detect indicators of possible fraud, such as altered signatures or information.

Department management should advise staff to immediately inform department management upon becoming aware of nonroutine or otherwise suspicious practices or circumstances with relation to a claim for benefits.

Department management should reemphasize its policies relating to the release of confidential information and the personal use of department equipment such as fax machines.

### **Management's Comment**

We concur with the finding and have taken steps to prevent such activity in the future.

1. Department management should further emphasize its employees' responsibilities regarding the safeguarding of computer passwords.

While all employees were given a copy of the department's Internal Security Handbook and were asked to sign a form stating they had read and understood the policy, Field Management staff feel we should communicate this policy to all personnel annually to emphasize its importance. This will be immediately communicated in writing to District Managers who will be expected to ensure that such a discussion is carried out in each of the local offices under their supervision. Additionally, I feel it is important to note that disciplinary action was taken against employees involved in this incident.

2. Department management should ensure that there are periodic reviews of claims initially rejected then later approved. Such reviews should be documented and maintained.

The Internal Audit Section and the UI Technical Support Sections are each receiving a report of claims that were initially denied and later approved. Staff members will review these reports and document the results of the reviews.

3. Field office supervisors should periodically review documents relating to claims to detect indicators of possible fraud, such as altered signatures or information.
4. Department management should advise staff to immediately inform department management upon becoming aware of nonroutine or otherwise suspicious practices or circumstances with relation to a claim for benefits.

The local offices already have a quality control process whereby all claims material is checked for accuracy before being forwarded to central office. The local office manager frequently handles this though sometimes another staff member is assigned this responsibility. If a staff member notices something that appears questionable during this review process, I feel that person would call it to the supervisor's attention. However, we will stress this aspect of the policy to field staff at the time we review the Internal Security Handbook with them.

5. Department management should reemphasize its policies relating to the release of confidential information and the personal use of department equipment such as fax machines.

In November 1998 at a statewide managers meeting, a guide was given to all local office managers to assist field staff in properly releasing confidential information. A memorandum from upper management dated December 9, 1998, followed this providing additional information in this area.

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### **Nashville Special Projects Office**

On May 4, 1999, the internal auditor of the Department of Labor (now called the Department of Labor and Workforce Development) notified the Division of State Audit about information the department had received regarding the manager of the Nashville Special Projects

(NSP) Office. The information alleged that the manager was improperly using state office equipment and resources on behalf of his second job as Sports Information Director for Fisk University. Moreover, it was alleged that the manager operated an employment agency, on state time and using state resources, to find jobs for his friends and other individuals who were not department clients. These individuals were primarily from Fisk University, Tennessee State University, and Pearl-Cohn High School, all located in Nashville, Tennessee. Further, it was alleged that the manager allowed these nonclients to use state equipment such as computers, printers, telephones, a fax machine, and a copier; state-issued bus passes; and state supplies, such as copy paper. It was also alleged that the presence of these individuals in department offices significantly disrupted the work of other office staff. On May 6, 1999, Division of State Audit staff in collaboration with the department's internal audit staff began a review of the matter. A special report on the results of the review was released on February 1, 2000.

The objectives of the review were

- to determine the nature and extent of any impropriety relating to the misuse of the NSP office by the manager;
- to determine if the manager held employment outside the department;
- to determine if the manager operated an employment agency using NSP resources;
- to determine if the manager allowed access to state resources and equipment to unauthorized individuals;
- to report the results of the review to department management; and
- to refer the results of our review to the Office of the State Attorney General and other relevant state agencies, if necessary.

The review included interviews with NSP office personnel, department management, and Fisk University staff. The review included an examination of the Tennessee Department of Employment Security *Internal Security Handbook*, which detailed the department's policies relating to properly reporting second jobs and to the use of state equipment. The auditors also reviewed telephone logs for the period April 1, 1998, through March 25, 1999, and fax logs (for several days) that were obtained from the NSP office, as well as a directory listing obtained from the manager's state computer located in his work area at the NSP office.

The review determined that the manager held a second job as Sports Information Director for Fisk University and that he also wrote sports-related articles for the *Nashville Pride* newspaper, but had not disclosed his outside employment to the department, as required by department policy. The manager admitted that he had used his state computer to maintain sports statistics related to his second job as Sports Information Director and to write newspaper articles for the *Nashville Pride* newspaper. The review further determined that the manager had used the state telephone system to make personal long-distance telephone calls. The cost attributable to his personal long-distance telephone calls for the period April 1, 1998, through March 25, 1999, was \$53.29. Further, the manager admitted that he had used the office fax machine on an infrequent basis for personal business, such as faxing his articles to the *Nashville Pride*.

The review also determined that the manager had used his position to operate an employment placement service, from the NSP office, for his friends and other individuals who were not department clients, in violation of his role and responsibility to provide services to department clients only. The manager acknowledged that he had operated an employment service for nonclients using state resources, and he provided the rationale that he was acting pursuant to his personal belief that he needed to do what he could to prevent individuals from having to obtain food stamps and unemployment benefits. The manager admitted that he had allowed these individuals, who were not state employees and who were not department clients, the use of state equipment and supplies to make telephone calls, send faxes, and prepare and print resumes. He also confirmed that he had provided some state-issued bus passes to these individuals. The manager told the auditors that he did not receive any money from any person or organization for providing these employment services to these individuals.

The department's corrective actions included demoting the manager from the classification of Employment Security Manager I to the classification of Employment Security Interviewer II, effective August 16, 1999. The manager was suspended for five workdays without pay, effective August 17, 1999; and his salary was decreased two steps, effective August 17, 1999. Further, the manager was transferred from the NSP office to the Nashville Metro Office, effective August 25, 1999. On November 2, 1999, the office manager paid \$53.29 to the department in full repayment for his personal long distance telephone calls.

**3. Weaknesses in supervision and monitoring enabled a department manager to abuse his position**

**Finding**

The manager had signed an acknowledgment form on October 19, 1998, which stated that he had read, understood, and would abide by the department's policies. The *Internal Security Handbook* policies related to secondary employment and proper use of state equipment, supplies, and other resources, such as office space and work time. However, the manager disregarded the department's policies, as detailed above.

Internal control policies and procedures are essential for government services to function well. Equally important are staff who know, understand, and implement those policies and procedures. Especially critical are the activities of senior-level staff, such as office managers, because senior-level staff constitutes the department's control points in implementing and enforcing policies and procedures.

Top management may have the reasonable expectation that staff at the mid-management level should know, understand, and abide by department policies. However, top management should also weigh such factors as the decentralized nature of its offices and the physical separation between office managers and their immediate supervisors. In those situations, top

management should consider the need for increased supervision, training, on-site monitoring, and audits.

The review disclosed four internal control weaknesses. First, because the manager was responsible for a separate office, his activities were not sufficiently monitored by his direct supervisor, who worked in another building. This lack of effective monitoring allowed the manager to engage in unauthorized activities at his office and during working hours and to disrupt the work of other department employees. Second, office telephone calls were not subjected to the type of review that would disclose unauthorized personal long distance telephone calls. Therefore, the manager was able to make these calls over the one-year period without detection. Third, the department did not maintain effective control over bus passes. The manager was not required to maintain a list of who received bus passes or to reconcile the bus passes provided to the NSP office for distribution. Fourth, although NSP office staff had been informed that all inappropriate activities should be reported to appropriate department staff, and although the manager's activities were long-standing, significant time elapsed before the department received information indicating that the manager was engaged in unauthorized activities. The reluctance of NSP office staff to inform department management of apparent improprieties indicates that the department's procedures for reporting confidential complaints need to be reemphasized.

### **Recommendation**

The department should formally communicate to all NSP office staff that NSP office resources are to be used only for their intended purposes. The formal written communication should reemphasize that under no circumstances are state resources to be used for personal purposes. These resources include, but are not limited to, computers, telephones, fax machines, copiers, supplies, and bus passes.

The department should take immediate steps to stop any abuse of state office space and time at the NSP office by reemphasizing the office's mission and client focus and by enforcing visitor sign-in requirements.

The department should immediately develop and implement policies and procedures for making confidential formal complaints against management-level staff and distribute the policy to all staff.

The department should establish a sign-out log for bus passes and separate the functions of distributing the bus passes and maintaining primary custody of the bus passes. The department should also periodically reconcile bus passes distributed to bus passes on hand.

## Management's Comment

We concur with the finding and have taken necessary steps to prevent future occurrences of this nature.

1. The department should formally communicate to all NSP office staff that NSP office resources are to be used only for their intended purposes.

A meeting was held with the staff to review the department's Internal Security policy. In that meeting the local office manager responsible for this unit stressed all aspects of the policy, pointing out that State resources were to be used strictly for State-related purposes and only by State employees.

2. The department should to take immediate steps to stop any abuse of state office space and time at the NSP office by reemphasizing the office's mission and client focus and by enforcing visitor sign-in requirements.

This was also stressed during the meeting with all employees of this unit during the meeting noted above.

3. The department should immediately develop and implement policies and procedures for making confidential formal complaints against management-level staff and distribute the policy to all staff.

The department's current Internal Security policy includes such procedures, but we feel we should reinforce this to all field staff when we review the policy with them.

4. The department should establish a sign-out log for bus passes and separate the functions of distributing the bus passes and maintaining primary custody of the bus passes. The department should also periodically reconcile bus passes distributed to bus passes on hand.

Procedures have been implemented whereby one individual maintains the numbered passes under lock and key. When staff members have clients who are eligible and in need of bus passes, that staff member must go to the Interviewer in charge of these and sign a log showing which number(s) they have checked out. Then the client receiving a pass must sign a log by the number of the bus pass he/she has been given. All records are maintained in the Nashville Special Projects office for the designated period of time for audit purposes.

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## **PRIOR AUDIT FINDING**

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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 to implement the recommendations in the prior audit report. A follow-up of the prior audit finding was conducted as part of the current audit.

## **RESOLVED AUDIT FINDING**

The current audit disclosed that the Department of Employment Security has corrected the previous audit finding concerning cash management.

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## **OBSERVATIONS AND COMMENTS**

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### **TITLE VI OF THE CIVIL RIGHTS ACT OF 1964**

*Tennessee Code Annotated*, Section 4-21-901, 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, 1994, and each June 30 thereafter. For the year ending June 30, 1999, the Department of Employment Security filed its compliance report and implementation plan on June 30, 1999.

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.

On October 15, 1998, the Commissioner of Finance and Administration notified all cabinet officers and agency heads that the Human Rights Commission is the coordinating state agency for the 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.

## **TITLE IX OF THE EDUCATION AMENDMENTS OF 1972**

*Tennessee Code Annotated*, Section 4-4-123, requires each state governmental entity subject to the requirements of Title IX of the Education Amendments of 1972 to submit an annual Title IX compliance report and implementation plan to the Department of Audit by June 30, 1999, and each June 30 thereafter. The Department of Employment Security did not file its compliance report and implementation plan by June 30, 1999, in violation of this statutory requirement.

Title IX of the Education Amendments of 1972 is a federal law. The act requires all state agencies receiving federal money to develop and implement plans to ensure that no one receiving benefits under a federally funded education program and activity is discriminated against on the basis of gender. Because the department did not file the compliance report and implementation plan required by state law does not necessarily mean that the Department of Employment Security is not in compliance with federal law.

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## **APPENDIX**

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### **DIVISIONS AND ALLOTMENT CODES**

Department of Employment Security divisions and allotment codes:

331.01 Division of Administration  
333.03 Deferred Revenue  
333.09 Trust Fund