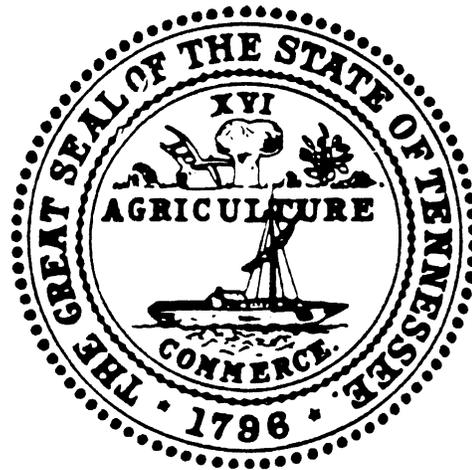


# AUDIT REPORT

East Tennessee Community Services Agency

August 2007



STATE OF TENNESSEE  
COMPTROLLER OF THE TREASURY

Department of Audit  
Division of State Audit



***Arthur A. Hayes, Jr., CPA, JD, CFE***  
Director

***Edward Burr, CPA***  
Assistant Director

***Teresa L. Kennedy, CPA***  
Audit Manager

***Kimberly D. White***  
In-Charge Auditor

***Jon Cheek***  
Staff Auditor

***Amy Brack***  
Editor

Comptroller of the Treasury, Division of State Audit  
1500 James K. Polk Building, Nashville, TN 37243-0264  
(615) 401-7897

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**STATE OF TENNESSEE**  
**COMPTROLLER OF THE TREASURY**

State Capitol  
Nashville, Tennessee 37243-0260  
(615) 741-2501

**John G. Morgan**  
Comptroller

August 16, 2007

The Honorable Phil Bredesen, Governor  
and  
Members of the General Assembly  
State Capitol  
Nashville, Tennessee 37243  
and  
Board of Directors  
East Tennessee Community Services Agency  
201 Center Park Drive  
Suite 1100  
Knoxville, Tennessee 37922

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the East Tennessee Community Services Agency for the period March 1, 2006, through January 31, 2007.

The review of internal control and compliance with laws, regulations, and provisions of contracts or grant agreements resulted in no audit findings.

Sincerely,

John G. Morgan  
Comptroller of the Treasury

JGM/tlk  
07/062



STATE OF TENNESSEE  
**COMPTROLLER OF THE TREASURY**  
DEPARTMENT OF AUDIT  
DIVISION OF STATE AUDIT

SUITE 1500  
JAMES K. POLK STATE OFFICE BUILDING  
NASHVILLE, TENNESSEE 37243-0264  
PHONE (615) 401-7897  
FAX (615) 532-2765

February 8, 2007

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

Dear Mr. Morgan:

We have conducted a financial and compliance audit of selected programs and activities of the East Tennessee Community Services Agency for the period March 1, 2006, through January 31, 2007.

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

Our audit resulted in no audit findings. We have reported other less significant matters involving the agency's internal control to the East Tennessee Community Services Agency's management in a separate letter.

Sincerely,

Arthur A. Hayes, Jr., CPA  
Director

AAH/tlk

State of Tennessee

# Audit Highlights

Comptroller of the Treasury

Division of State Audit

Financial and Compliance Audit  
**East Tennessee Community Services Agency**  
August 2007

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## AUDIT SCOPE

We have audited the East Tennessee Community Services Agency for the period March 1, 2006, through January 31, 2007. Our audit scope included a review of internal control and compliance with laws, regulations, and provisions of contracts or grant agreements in the areas of cash and cash receipts, and expenditures. The audit was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include approving accounting policies of the state as prepared by the state's Department of Finance and Administration; approving certain state contracts; participating in the negotiation and procurement of services for the state; and approving the Community Services Agencies' Plans of Operation (budgets).

## AUDIT FINDINGS

The audit report contains no findings.

# Financial and Compliance Audit East Tennessee Community Services Agency

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# **Financial and Compliance Audit East Tennessee Community Services Agency**

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## **INTRODUCTION**

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### **POST-AUDIT AUTHORITY**

This is the report on the financial and compliance audit of the East Tennessee Community Services Agency. The audit was conducted pursuant to Section 37-5-313, *Tennessee Code Annotated*, which authorizes the Comptroller of the Treasury to “make an annual audit of the program established by this part as part of the comptroller’s annual audit pursuant to Section 9-3-211.”

### **BACKGROUND**

The Community Services Agency Act of 1996 created the community services agencies. The purpose of these agencies is to coordinate funds and programs designated for care of children and other citizens in the state.

The East Tennessee Community Services Agency serves the following counties: Anderson, Blount, Campbell, Claiborne, Cocke, Grainger, Hamblen, Jefferson, Knox, Loudon, Monroe, Morgan, Roane, Scott, Sevier, and Union. The agency’s administrative offices are in Knoxville, Tennessee.

The governing body of the East Tennessee Community Services Agency is the board of directors. As of January 31, 2007, the board was composed of ten members. (See Appendix.) An executive committee, consisting of four board members, has the authority to act on behalf of the board of directors in the management of the agency’s property, affairs, and funds in extraordinary circumstances when the governing board cannot convene.

The agency’s programs are carried out by staff under the supervision of the executive director, who was appointed by the Commissioner of the Department of Children’s Services, subject to the approval of the board.

In September 2005, the agency contracted with the Department of Finance and Administration to conduct case management for the Interim Shelter Program. This program’s purpose was to assist families who were evacuated from coastal areas of Louisiana, Mississippi, and Alabama as a result of Hurricane Katrina and Hurricane Rita. This program ended on June 30, 2006.

In March 2006, the agency also entered into an agreement with the Department of Finance and Administration's Division of Mental Retardation Services to provide support coordination services for Medicaid eligible enrollees in the Home and Community Based Services Waiver for the Mentally Retarded and Developmentally Disabled. The agency's Independent Support Coordination Program assists enrollees by identifying, selecting, obtaining, coordinating, and using services to enhance the enrollees' independence, integration in the community, and productivity in the community. As of February 8, 2007, the agency was serving 102 recipients.

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## AUDIT SCOPE

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We have audited the East Tennessee Community Services Agency for the period March 1, 2006, through January 31, 2007. Our audit scope included a review of internal control and compliance with laws, regulations, and provisions of contracts or grant agreements in the areas of cash and cash receipts, and expenditures. The audit was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include approving accounting policies of the state as prepared by the state's Department of Finance and Administration; approving certain state contracts; participating in the negotiation and procurement of services for the state; and approving the Community Services Agencies' Plans of Operation (budgets).

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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 taken to implement the recommendations in the prior audit report. The East Tennessee Community Services Agency filed its report with the Department of Audit on December 21, 2006. A follow-up of the prior audit finding was conducted as part of the current audit. The current audit disclosed that the East Tennessee Community Services Agency has corrected the previous audit finding concerning bank reconciliations not being prepared.

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## OBJECTIVES, METHODOLOGIES, AND CONCLUSIONS

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### CASH AND CASH RECEIPTS

The primary objectives of our review of cash and cash receipts were to determine whether

- the design of the agency's controls over cash and cash receipting was adequate;
- the agency deposited funds promptly in accordance with policy;
- cash receipts were posted correctly to the accounting records;
- revenue for a selected month for the Independent Support Coordination Program agreed to both related amounts deposited into the agency's Local Government Investment Pool account and billings to the Division of Mental Retardation Services based on the number of recipients served; and
- bank reconciliations were accurate and performed promptly.

To accomplish our objectives, we interviewed management to gain an understanding of the agency's procedures and controls over cash and cash receipts. We obtained the cash receipts for March 1, 2006, through January 31, 2007, and tested a non-statistical sample of cash receipts for timeliness of deposit in accordance with policy and proper posting to the accounting records. We also obtained a listing from management of all revenue received for the Independent Support Coordination Program from the inception of the program through December 31, 2006. We agreed the revenue received for November 2006 to both the related amounts deposited into the agency's Local Government Investment Pool account and billings to the Division of Mental Retardation Services based on the number of recipients served. In addition, we obtained all bank reconciliations for March 2006 through December 2006 to ensure they were performed promptly. We performed detailed testwork on the March 2006 reconciliation to ensure its accuracy.

As a result of interviews and testwork performed, we determined that

- the agency's controls over cash and cash receipting were adequately designed;
- the agency deposited funds promptly in accordance with policy;
- cash receipts were posted correctly to the accounting records;
- revenue for the month selected for the Independent Support Coordination Program agreed to both related amounts deposited into the agency's Local Government Investment Pool account and billings to the Division of Mental Retardation Services based on the number of recipients served; and
- bank reconciliations were performed promptly, with minor exceptions noted, and the reconciliation tested was accurate.

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## EXPENDITURES

Our primary objectives were to determine whether

- the design of the agency's controls over expenditures was adequate;
- expenditures for goods or services were properly approved, supported, and allowable under applicable program guidelines;
- goods were received or services were rendered prior to payment;
- expenditures for travel were paid in accordance with the Comprehensive Travel Regulations;
- the agency's policies and procedures for credit cards were adequate and credit card purchases were reasonable; and
- the agency's plan of operation and amendments were properly approved.

To accomplish our objectives, we interviewed key agency personnel to gain an understanding of procedures and controls over expenditures. We also reviewed written policies and procedures. We obtained the agency's check register for March 1, 2006, through January 31, 2007, and tested a non-statistical sample of expenditures to determine that they were approved, supported, and allowable under the applicable guidelines of programs administered by the agency and that the related goods were received or services were rendered prior to payment. We tested a non-statistical sample of travel expenditures from March 1, 2006, through January 31, 2007, for compliance with the Comprehensive Travel Regulations. We also tested all of the Executive Director's travel claim expenditures for compliance with the Comprehensive Travel Regulations for the same time period. We discussed policies and procedures for credit card purchases with staff. In addition, we obtained all credit card statements for our audit period and reviewed the purchases contained therein for reasonableness. Finally, we obtained the plan of operation and related amendments to determine the appropriateness of approvals.

As a result of interviews and testwork performed, we determined that

- the agency's controls over expenditures were adequately designed;
- expenditures for goods or services were properly approved, supported, and allowable under applicable program guidelines;
- goods were received or services were rendered prior to payment;
- expenditures for travel were paid in accordance with the Comprehensive Travel Regulations;
- the agency's policies and procedures for credit cards were adequate and credit card purchases were reasonable; and
- the plan of operation and amendments were properly approved.

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## **OBSERVATIONS AND COMMENTS**

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### **MANAGEMENT'S RESPONSIBILITY FOR RISK ASSESSMENT**

Auditors and management are required to assess the risk of fraud in the operations of the entity. The risk assessment is based on a critical review of operations considering what frauds could be perpetrated in the absence of adequate controls. The auditors' risk assessment is limited to the period during which the audit is conducted and is limited to the transactions that the auditors are able to test during that period. The risk assessment by management is the primary method by which the entity is protected from fraud, waste, and abuse. Since new programs may be established at any time by management or older programs may be discontinued, that assessment is ongoing as part of the daily operations of the entity.

Risks of fraud, waste, and abuse are mitigated by effective internal controls. It is management's responsibility to design, implement, and monitor effective controls in the entity. Although internal and external auditors may include testing of controls as part of their audit procedures, these procedures are not a substitute for the ongoing monitoring required of management. After all, the auditor testing is limited and is usually targeted to test the effectiveness of particular controls. Even if controls appear to be operating effectively during the time of the auditor testing, they may be rendered ineffective the next day by management override or by other circumventions that, if left up to the auditor to detect, will not be noted until the next audit engagement and then only if the auditor tests the same transactions and controls. Furthermore, since staff may be seeking to avoid auditor criticisms, they may comply with the controls during the period that the auditors are on site and revert to ignoring or disregarding the control after the auditors have left the field.

The risk assessments and the actions of management in designing, implementing, and monitoring the controls should be adequately documented to provide an audit trail both for auditors and for management, in the event that there is a change in management or staff, and to maintain a record of areas that are particularly problematic. The assessment and the controls should be reviewed and approved by the head of the entity.

### **FRAUD CONSIDERATIONS**

Statement on Auditing Standards No. 99, *Consideration of Fraud in a Financial Statement Audit*, promulgated by the American Institute of Certified Public Accountants requires auditors to specifically assess the risk of material misstatement of an audited entity's financial statements due to fraud. The standard also restates the obvious premise that management, not the auditors, is primarily responsible for preventing and detecting fraud in its own entity. Management's responsibility is fulfilled in part when it takes appropriate steps to assess the risk of fraud within the entity and to implement adequate internal controls to address the results of those risk assessments.

During our audit, we discussed these responsibilities with management and how management might approach meeting them. We also increased the breadth and depth of our inquiries of management and others in the entity as we deemed appropriate. We obtained formal assurances from top management that management had reviewed the entity's policies and procedures to ensure that they are properly designed to prevent and detect fraud and that management had made changes to the policies and procedures where appropriate. Top management further assured us that all staff had been advised to promptly alert management of all allegations of fraud, suspected fraud, or detected fraud and to be totally candid in all communications with the auditors. All levels of management assured us there were no known instances or allegations of fraud that were not disclosed to us.

## **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 East Tennessee Community Services Agency establish an audit committee. The board chair of the CSA initially appointed a three-member committee on January 13, 2005. The entire board appointed the audit committee on June 27, 2006. The audit committee charter was approved by the Comptroller of the Treasury on June 12, 2006. Additionally, the audit committee approved a written code of conduct and a new conflict-of-interest statement for the agency and provided copies of each to agency management and staff. On December 12, 2006, the audit committee and the board of the CSA approved the fraud risk assessment prepared by management of the agency.

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**APPENDIX**

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**EAST TENNESSEE COMMUNITY SERVICES AGENCY**

Mr. Mike Harkleroad, Executive Director

**BOARD OF DIRECTORS**

As of January 31, 2007

**Executive Committee**

Mr. Eddie Davis, Chairperson  
Mr. James Gaddis, Vice Chairperson  
Ms. Sherrie Claiborne, Treasurer  
Mr. Robert Webb, Secretary

**Audit Committee**

Mr. James Gaddis, Chairperson  
Ms. Sherrie Claiborne  
Mr. Robert Webb

**Other Members of the Board of Directors**

Ms. Flo Charles  
Ms. Paula Gibson  
Ms. Anne Phillips  
Ms. Nancy Rader  
Ms. Ann Richardson  
Mr. Richard Thomas