

**DEPARTMENT OF COMMERCE AND INSURANCE**

**FOR THE YEARS ENDED  
JUNE 30, 1995, AND JUNE 30, 1994**

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April 3, 1997

The Honorable Don Sundquist, Governor  
and

Members of the General Assembly  
State Capitol  
Nashville, Tennessee 37243

and

The Honorable Douglas M. Sizemore, Commissioner  
Department of Commerce and Insurance  
500 James Robertson Parkway  
Nashville, Tennessee 37243

Ladies and Gentlemen:

Transmitted herewith is the compliance audit of the Department of Commerce and Insurance for the years ended June 30, 1995, and June 30, 1994.

Consideration of the internal control structure and tests of compliance disclosed certain deficiencies, which are detailed in the Results of the Audit section of this report. The department's administration has responded to the audit findings; the responses are included following each finding. The Division of State Audit will follow up the audit to examine the application of the procedures instituted because of the audit findings.

Very truly yours,

W. R. Snodgrass  
Comptroller of the Treasury

WRS/cr  
96/072

State of Tennessee

# Audit Highlights

Comptroller of the Treasury

Division of State Audit

Compliance Audit

**Department of Commerce and Insurance**

For the Years Ended June 30, 1995, and June 30, 1994

## AUDIT OBJECTIVES

The objectives of the audit were to consider the department's internal control structure; to test compliance with certain laws, regulations, contracts, or grants; and to recommend appropriate actions to correct any deficiencies.

## INTERNAL CONTROL FINDINGS

### **Improvement Needed in Electrical Inspection Procedures\***

Inspectors are allowed to collect permit fees as well as issue inspection reports. Reconciliation of the inventory listing of permits and inspection reports issued with permit fees received and with inspection fees paid to inspectors is not performed regularly. In addition, evaluations of inspectors and follow-ups of their work are not done in a timely manner. There is not adequate documentation that inspectors are taking the National Certification exam as often as required. Furthermore, inspection reports are some-

times issued earlier than five working days after the issuance of the permit in violation of departmental rule (page 11).

### **Timesheet and Leave Approval Procedures Not Followed**

In some instances, timesheets were signed by time-keepers without proper documentation from the employee. Additionally, some leave requests were signed by someone other than the employee (page 15).

## COMPLIANCE FINDINGS

### **Inadequate Monitoring Procedures at the Burial Services Board**

When cemeteries either pay late or do not pay registration fees, no penalties are assessed. Additionally, no penalties are assessed for cemeteries that do not submit the required reports or meet trust requirements (page 9).

### **Applications for Funeral Directors and Embalmers Inadequate**

Applications for funeral directors and embalmers do not request all the information and disclosures required by state law (page 11).

\* This finding is repeated from the prior four audits.

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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  
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AUDIT REPORT  
DEPARTMENT OF COMMERCE AND INSURANCE  
FOR THE YEARS ENDED JUNE 30, 1995, AND JUNE 30, 1994

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DEPARTMENT OF COMMERCE AND INSURANCE  
FOR THE YEARS ENDED JUNE 30, 1995, AND JUNE 30, 1994

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INTRODUCTION

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**POST-AUDIT AUTHORITY**

This is a report on the compliance audit of the Department of Commerce and Insurance. 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.

**OBJECTIVES OF THE AUDIT**

The objectives of the audit were

1. to consider the department’s internal control structure to determine auditing procedures for the purpose of testing compliance with certain laws, regulations, contracts, or grants;
2. to test compliance with certain laws, regulations, contracts, or grants; and
3. to recommend appropriate actions to correct any deficiencies.

**SCOPE OF THE AUDIT**

The audit is limited to the period July 1, 1993, through June 30, 1995, and was conducted in accordance with generally accepted government auditing standards.

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## BACKGROUND AND ORGANIZATION

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### LEGISLATIVE HISTORY

The Bureau of Insurance was established by legislative enactment in 1873. The State Treasurer served *ex officio* as Commissioner of Insurance. In 1913, a separate Department of Insurance was formed and put under the direction of a commissioner, who became an officer in the Governor's cabinet. The name of the department was changed to the Department of Commerce and Insurance in 1983.

### ORGANIZATION

The Department of Commerce and Insurance is headed by a commissioner who reports directly to the Governor. The commissioner is assisted by two deputy commissioners, a legal services section, an internal audit section, and seven divisions. Below is a description of each division.

The Division of Administration is the central planning and coordinating division of the Department of Commerce and Insurance. It is responsible for the coordination of all budgeting, recording, and summarizing activities within the department.

The Division of Insurance is responsible for enforcing all insurance laws of the state and for supervising all life, casualty, and other insurance companies authorized to transact business in Tennessee.

The Division of Fire Prevention initiates statewide fire prevention programs; investigates the origin and circumstances of fires; inspects liquefied petroleum gas installations, fireworks dealerships, mobile home construction, and gasoline bulk plants and prosecutes violators of the pertinent statutes; supervises electrical inspections; and inspects public buildings for fire safety. The staff develops and maintains extensive public assembly programs, the media, and specialized training programs. The Tennessee Commission on Fire Fighting Personnel was transferred from the Division of Regulatory Boards in 1983.

The Division of Securities is responsible for enforcing all state laws pertaining to securities dealers and salesmen.

The Division of Consumer Affairs is responsible for enforcing the Consumer Protection Act. The division receives consumer complaints and inquiries, investigates them, and takes corrective action, if necessary.

The Division of Regulatory Boards is responsible for various boards and commissions. In general, these boards and commissions perform the occupational licensing and regulation of the professions in Tennessee subject to regulation, except those related to health care and protection of the environment. The Governor selects the members for appointment to the various boards from lists of names submitted by trades and professions. The charges and fees collected by the boards are deposited into the state's general fund, the fund from which the regulatory boards receive appropriations to cover their operating costs.

The Tennessee Claims Commission and the Tennessee Racing Commission are also boards of the Department of Commerce and Insurance; however, the Division of Regulatory Boards is not administratively responsible for them.

The Division of TennCare was created by the governor on January 26, 1995, and provides financial oversight of all TennCare managed care organizations (MCOs). The division's duties include examining and monitoring the MCOs for compliance with contractual requirements relating to financial responsibility, stability and integrity, and management operations.

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

The Department of Commerce and Insurance is part of the general fund of the State of Tennessee. The Real Estate Education and Recovery and Auctioneer Education Recovery funds are special revenue funds. The audit covered the following divisions and allotment codes:

335.01	Division of Administration
335.02	Division of Insurance
335.03	Division of Fire Prevention
335.04	Division of TennCare
335.05	Division of Securities
335.06	Division of Consumer Affairs
335.09	Tennessee Racing Commission
335.10	Division of Regulatory Boards
335.14	Workers' Compensation Insurance Fund Act of 1992
335.15	Real Estate Education and Recovery
335.16	Auctioneer Education and Recovery
335.17	Tennessee Board of Pharmacy
335.27	Tennessee Motor Vehicle Commission
335.28	Tennessee Commission on Fire Fighting Personnel
335.30	Tennessee Claims Commission



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## PRIOR AUDIT FINDINGS

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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 Department of Commerce and Insurance filed its report with the Department of Audit on August 30, 1995. A follow-up of all prior audit findings was conducted as part of the current audit.

### RESOLVED AUDIT FINDINGS

The current audit disclosed that the department has corrected previous audit findings concerning the need to draw grant funds timely, improve procedures in private protective services, strengthen licensing procedures in the Motor Vehicle Commission, to improve timely inspections in the pharmacy board, and to complete employee performance evaluations in the division of consumer affairs.

### REPEATED AUDIT FINDING

The prior audit report also contained a finding concerning the need to improve procedures for electrical inspectors. This finding has not been completely resolved and is repeated in this report.

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## RESULTS OF THE AUDIT

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### AUDIT CONCLUSIONS

#### Internal Control Structure

We considered the internal control structure to determine auditing procedures for the purpose of testing compliance with certain laws, regulations, contracts, or grants. The report on the internal control structure is on the following pages. Certain deficiencies, along with recommendations and management's responses, are detailed in the findings and recommendations, which follow the report on the internal control structure.

## Compliance with Laws and Regulations

With respect to the items tested, the department complied with the provisions of certain laws, regulations, contracts, or grants except for certain instances of noncompliance included in the findings and recommendations. The compliance report follows the findings and recommendations.

## **Report on the Internal Control Structure**

April 8, 1996

The Honorable W. R. Snodgrass  
Comptroller of the Treasury  
State Capitol  
Nashville, Tennessee 37243

Dear Mr. Snodgrass:

We have applied procedures to test the Department of Commerce and Insurance's compliance with the provisions of certain laws, regulations, contracts, or grants for the years ended June 30, 1995, and June 30, 1994, and have issued our report thereon dated April 8, 1996. We performed the procedures in accordance with generally accepted government auditing standards.

We considered the department's internal control structure in order to determine our procedures for the purpose of testing the department's compliance with certain laws, regulations, contracts, or grants and not to provide assurance on the internal control structure.

The Department of Commerce and Insurance's management is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

The Honorable W. R. Snodgrass  
April 8, 1996  
Page Two

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the department's ability to comply with laws, regulations, contracts, or grants. However, we did note the following deficiencies:

- Electrical inspection procedures need to be improved
- Timesheet and leave approval procedures are not always followed

These deficiencies are described in the Findings and Recommendations section of this report.

We also noted certain matters involving the internal control structure and its operation that we have reported to the department's management in a separate letter.

This report is intended for the information of the General Assembly of the State of Tennessee and management. However, this report is a matter of public record, and its distribution is not limited.

Sincerely,

Arthur A. Hayes, Jr., CPA, Director  
Division of State Audit

AAH/cr

## FINDINGS AND RECOMMENDATIONS

### THE BURIAL SERVICES BOARD'S MONITORING PROCEDURES ARE INADEQUATE

#### 1. FINDING:

The Board of Burial Services registers cemeteries, collects annual registration fees, maintains files, performs examinations of cemeteries and trusts, and investigates complaints. Fifty-eight of the 176 cemetery files tested (33%) revealed that owners were either late in paying or had not paid their registration fees. Of these 58 cemeteries, six did not pay their 1995 fees, and 52 were late paying their renewal fees; however, the board assessed no penalties.

Section 46-1-104(a-c) of *Tennessee Code Annotated* states that certificates of registration expire at the end of the registrant's fiscal year following the certificate's issuance, and they become invalid if not renewed. Renewals of certificates of registration may be applied for any time during the two months before the previous certificate's expiration date. Fees for late renewals are set by the commissioner for each month (or fraction thereof) the renewal is delayed. Section 46-1-103(a) notes that it is a Class C misdemeanor for a cemetery to operate without a certificate.

One of five cemetery files tested (20%) did not have a pre-need trust account for sales of pre-need merchandise and services as required by section 46-2-403, *Tennessee Code Annotated*. Although this cemetery did have an improvement care trust fund as required in section 46-2-301, the improvement care trust fund documents were not updated to reflect a change in ownership.

One of five files tested (20%) did not have financial reports for 1994 and 1995 or the Annual Report of Cemetery Improvement Care Fund for 1995, and no penalties were assessed.

*Tennessee Code Annotated*, Section 46-2-202, requires each cemetery company to file with the commissioner a report of its condition within 75 days of the end of the calendar or fiscal year. The trustee of the company's improvement care fund must also file a trust fund report with the commissioner within the same time frame. The owner of the cemetery company and/or the trustee of the improvement care fund who fails to file the annual report commits a Class C misdemeanor. The commissioner is required to notify the cemetery company owner by registered letter if either report is not received and may order a conditional suspension of the certificate if the report is not received within 15 days of the letter's receipt. Section 46-2-410 sets forth the standard penalties for late filings.

The board's failure to monitor cemetery companies' compliance with state law results in lost registration fees and penalties.

RECOMMENDATION:

Management of the Board of Burial Services should develop written policies and procedures for monitoring cemetery companies and enforcing their compliance with state law.

MANAGEMENT'S COMMENT:

We concur. Policies and Procedures have been implemented to correct the deficiencies noted as follows:

- To prevent erroneous assessment of late penalties to renewal registrants, a request to the Information Systems Section has been made to add a ten day grace period to renewal transactions. This will prevent delays in renewal registration for fees that are postmarked before or on the registration expiration date.
- The following procedures are being implemented to ensure compliance with *Tennessee Code Annotated* 46-1-104 (a-c) and 46-1-103 (a): Renewal notices are being sent 60 days in advance of the expiration date through the Regulatory Boards System; Second notices will be sent within 15 days of the expiration date if the renewal fee has not been received at that time; A request for an informal conference with the registrant will be made if renewal and penalties are not received within 30 days of the expiration date of the registration.
- Increased staffing has occurred in Burial Services which will enable more effective monitoring of cemetery companies.
- Burial Services has established a procedure for identifying late reports regarding the financial condition of cemetery companies. The provisions of *Tennessee Code Annotated* 46-2-204 and 46-2-410 (d) will be strictly enforced.

THE BOARD OF FUNERAL DIRECTORS AND EMBALMERS DOES NOT OBTAIN  
ALL NECESSARY INFORMATION FROM APPLICANTS

2. FINDING:

An examination of the current applications for licenses used by the Board of Funeral Directors and Embalmers revealed that not all required information is requested on the applications.

Sections 62-5-305(a)(2,3) and 62-5-307(b)(2,3), *Tennessee Code Annotated*, require the applications for funeral directors' and embalmers' licenses to show that the applicant is a citizen of the United States and is of good moral character. Additionally, Section 62-5-305(a)(4) requires the applications for funeral directors to show that the applicant is properly protected against communicable diseases. The applications used by the board do not require disclosure of this information.

If individuals are not required to provide all necessary information, individuals who are not in compliance with state law could be licensed.

RECOMMENDATION:

The board should revise the application to include the information required by *Tennessee Code Annotated*.

MANAGEMENT'S COMMENT:

We concur. The Board is currently revising the applications for licensure to ensure compliance with the requirements established by state law.

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ELECTRICAL INSPECTION PROCEDURES NEED TO BE IMPROVED

3. FINDING:

The department contracts with individuals in each county to inspect electrical wiring of construction and remodeling projects. Before undertaking electrical work, building contractors or other individuals must buy a permit from an inspector, a power supplier, or a qualified agent. The permit-issuing agent remits the money to the department. When the electrical work is completed, an inspector performs the inspection and completes a

report. The inspection report is matched with the permit, and the inspector is paid 80 percent of the permit fee. If the electrical work is not performed and inspected within two years, the contractor or other individual must purchase another permit.

As noted in the prior four audits, the department does not have adequate controls over the collection of electrical inspection and permit fees. Management concurred with the finding each year, but an examination of the procedures revealed that the following weakness remains.

Inspectors are allowed to collect permit fees in the field as well as issue the inspection reports. Because they do both, they could keep the money from the permit sales and later perform the inspections, bypassing the department. Consequently, the department would lose its 20 percent of the permit fees. Also, inspectors could submit falsified inspection reports to collect fees when they believed that an individual or building contractor who previously purchased a permit would not have an inspection within the two-year period.

Because former inspectors have committed this type of fraud in the past, management has attempted to segregate duties to the fullest extent practical. To compensate for the inability to fully segregate these duties, management has implemented a system of pre-numbered permit and inspection forms and a quarterly reconciliation of inspectors' forms with fees collected and paid. A reconciliation process could compensate for the lack of segregation of duties, but the current reconciliation process is not adequate. Although the inspectors are required to submit a quarterly inventory report of their form books, the Electrical Inspection Section only randomly reconciles the inventory report of form books with permit fees received from and payments made to inspectors. In addition, the inspectors' inventory reports do not provide enough information to perform an adequate reconciliation. The reports do not provide beginning or ending inventory and only require inspectors to list entire books of forms they have on-hand, not the specific range of pre-numbered forms used or on-hand. If the inspectors used forms for unauthorized purposes, the department would not detect it.

In addition to the weakness noted in prior audits, the following weaknesses were noted:

- a. The Electrical Inspection Section does not perform inspector evaluations in a timely manner. Memorandum EL-93-1, dated January 2, 1993, requires electrical inspectors to be evaluated at least twice a year. For six of ten inspectors whose files were tested (60%), evaluations were not performed twice a year from July 1, 1993, to January 18, 1995. Three inspectors had only one evaluation during this period, and three inspectors had no evaluations during the period. Memorandum EL-95-1, dated January 19, 1995, also requires electrical inspectors to be evaluated at least once every six months. For two of ten inspectors whose files were tested (20%), evalua-

tions were not performed every six months. Neither inspector had any evaluations from January 19 to June 30, 1995.

The Electrical Inspector Supervisors do not follow-up inspections as required by EL-93-1 and EL-95-1. According to EL-93-1, when follow-ups are performed in conjunction with evaluations, the supervisor shall select at least one inspection report completed within the week prior to the evaluation and verify that the electrical approval/rejection decal was properly completed and applied. According to EL-95-1, the supervisor shall select at least two inspection reports completed within the two weeks prior to the evaluation and verify that the electrical approval/rejection decal was properly completed and applied. For four of ten inspectors whose files were tested (40%), the supervisor did not review the proper number of inspection reports. Two of these inspectors' files did not contain any follow-ups for the audit period, and in one inspector's file the supervisor reviewed no particular inspection report but commented that he had reviewed this inspector's work for several years.

- b. According to Standard Operating Procedure HE-DEI-1, B8, effective July 1, 1993, "the Deputy Electrical Inspector shall take the National Certification Exam for 1 & 2 Family Dwellings within one year of his appointment date. The Inspector shall continue to take the exam at least once per year until the Inspector passes the exam." Three of five inspectors' files tested (60%) contained no documentation that the inspector had taken the exam.
- c. According to departmental rule 0780-2-1.05, "The permit must be secured in the area where the work is to be performed at least five working days prior to requesting the inspection." It was noted during the audit that inspection reports are sometimes issued less than five working days after the issuance of the permit, and some inspection reports are issued the same day as the permit.

#### RECOMMENDATION:

The department should strengthen procedures for electrical inspectors. The department should perform complete and timely reconciliations of the inspectors' inventory reports. Each inspector should provide the department with a specific statement of beginning inventory, permits or inspection forms issued, new permits or inspection forms received from the department, voided permits or inspection forms, and ending inventory on-hand. The department should compare the beginning inventory to the prior ending inventory, permits issued to fees collected, inspection reports issued to fees paid to inspectors, and new forms received to forms distributed by the department.

The department should implement procedures to ensure that evaluations are performed timely and that the proper number of follow-ups are performed by supervisors. The department should maintain documentation to ensure that inspectors take the National Certification Exam for 1 & 2 Family Dwellings as required. Also, the department should implement procedures to ensure that inspections are performed at least five working days after the issuance of the permit or modify the departmental rule if a five day period between the permit issuance and the inspection is no longer considered necessary.

MANAGEMENT'S COMMENT:

We concur. The department has taken the following actions to correct the deficiencies noted:

- The department has created a task force to review the current processes for electrical permit issuance and electrical inspections. This task force will specifically address deficiencies noted in the audit report and will provide recommendations for corrective action.
- Although inspectors in some areas continue to collect permit fees, it should be noted that the department has actively recruited issuing agents in all counties to eliminate inspectors from the permit issuance process. Issuing agents should be established in all areas within the next four months.
- Due to the obsolescence of the current permit tracking system and the massive volume of permits issued, complete reconciliations of permit inventories, revenues, and issuance is labor intensive and impractical. The department recently received funding to modify/replace the existing computer system and permit and inspection reconciliations will be paramount in the review by the task force.
- In May 1996, a new evaluation tracking system was developed to ensure that all evaluations are performed in a timely manner. Additionally, Policy EL-97-01 has been issued and requires that inspectors be evaluated annually rather than biannually. As part of the evaluation, the department has developed a log documenting inspection dates and follow-ups associated with those dates.
- Documentation of results of the National Certification Exam for 1 & 2 Family Dwellings is now required regardless of whether the exam is successfully completed.
- In accordance with the revised electrical regulations which are effective March 1997, permits are no longer required to be secured in the area five days prior to the inspection.

TIMESHEET AND LEAVE APPROVAL PROCEDURES ARE NOT  
ALWAYS FOLLOWED

4. FINDING:

An audit of payroll records revealed that timesheets and leave requests are not always properly signed. A policy established February 16, 1994, says that the timekeeper may sign an Attendance and Leave Form for field employees if employees submit a signed Field Attendance and Leave Report certifying their attendance and leave record each pay period. Employees requesting leave must, without exception, sign the Employee Leave Request Form.

An examination of payroll and personnel files at various boards and divisions revealed that for four of 38 employee files tested (11%), the Attendance and Leave Forms were not signed or approved with the proper documentation. In these instances, the timekeeper at the board or division signed for the employee without requiring a Field Attendance and Leave Report from the employee as supporting documentation. For these four employees, this occurred in 64% to 100% of the 33 pay periods during the audit period.

It was also noted that for four of 38 employees whose files were tested (11%), the files had Employee Leave Request Forms signed by someone else or had no signature at all.

If timesheets and leave requests are approved without proper signatures or supporting documentation, time may be recorded incorrectly, and employees could be paid for time not worked or dispute their attendance and leave records.

RECOMMENDATION:

Departmental policies have been established by management to provide adequate documentation and approval for payroll. Management should ensure that these established policies are followed.

MANAGEMENT'S COMMENT:

We concur. The Personnel Office was unaware of the existence of the "Signature Requirements for Attendance and Leave Forms" memo dated February 16, 1994. Effective July 1, 1996, the department implemented the Data Capture System for recording leave and attendance and new guidelines and procedures have been established to ensure that all policies and procedures are complied with.

## Compliance Report

April 8, 1996

The Honorable W. R. Snodgrass  
Comptroller of the Treasury  
State Capitol  
Nashville, Tennessee 37243

Dear Mr. Snodgrass:

We have applied procedures to test the Department of Commerce and Insurance's compliance with the provisions of certain laws, regulations, contracts, or grants for the years ended June 30, 1995, and June 30, 1994. We performed the procedures in accordance with generally accepted government auditing standards.

Compliance with laws, regulations, contracts, or grants applicable to the Department of Commerce and Insurance is the responsibility of the department's management. Our objective was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

The results of our tests indicate that the Department of Commerce and Insurance complied with the provisions referred to in the preceding paragraph, except for certain instances of noncompliance included in the Findings and Recommendations section of this report. We also noted other less significant instances of noncompliance that we have reported to the department's management in a separate letter.

This report is intended for the information of the General Assembly of the State of Tennessee and management. However, this report is a matter of public record and its distribution is not limited.

Sincerely,

Arthur A. Hayes, Jr., CPA, Director  
Division of State Audit

AAH/cr