



State of Tennessee

# DEPARTMENT OF AUDIT

## 2011 ANNUAL REPORT



Justin P. Wilson  
Comptroller of the Treasury



**Comptroller of the Treasury**  
**Justin P. Wilson**

**Department of Audit**

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STATE OF TENNESSEE  
COMPTROLLER OF THE TREASURY

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Justin P. Wilson  
Comptroller

December 29, 2011

The Honorable Governor Bill Haslam  
The Honorable Ron Ramsey, Speaker of the Senate  
The Honorable Beth Harwell, Speaker of the House of Representatives, and  
Members of the General Assembly  
State Capitol  
Nashville, Tennessee 37243

Ladies and Gentlemen:

The 2011 annual report of the Department of Audit is submitted herewith in accordance with Section 4-3-304 of *Tennessee Code Annotated*.

The Department of Audit conducts audits or ensures that audits are conducted of state, county, and municipal governments; utility districts; internal school funds; and other local government authorities and agencies. Audits are also performed of state grants to nongovernmental organizations and of numerous federal programs for state and local governments.

In submitting this report, I would like to express my appreciation to all those who made possible the results reported, particularly the members of the General Assembly and the staff of this office.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Justin P. Wilson".

Justin P. Wilson  
Comptroller of the Treasury

JPW/ab



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# Department of Audit

## 2011 Annual Report

The General Assembly created the Department of Audit in 1937. Authority to audit state and county governmental entities is contained primarily in Section 4-3-304, *Tennessee Code Annotated*. The department is required to:

- perform currently a post-audit of all accounts and financial records of the state government . . . in accordance with generally accepted auditing standards and . . . such procedures as may be established by the comptroller . . .
- make annually, and at such other times as the general assembly shall require, a complete report on the post audit . . .
- certify to the fund balance sheets, operating and other statements, covering the condition of the state's finances, as prepared by the department of finance and administration, or by the state treasurer, before publication of such statements . . .
- serve as a staff agency to the general assembly, or to any of its committees, in making investigations of any phase of the state's finances . . .
- make annually an audit of all the records of the several counties of the state . . .
- perform economy and efficiency audits, program results audits and program evaluations . . .
- require that audits to be performed by the internal audit staffs of grantees or the internal audit staffs of state departments, boards, commissions, institutions, agencies, authorities or other entities of the state shall be coordinated with the office of the comptroller of the treasury . . . in accordance with standards established by the comptroller . . .
- require that all persons, corporations or other entities who receive grants from or through this state shall cause a timely audit to be performed, in accordance with auditing standards prescribed by the comptroller . . .

The Department of Audit comprises three divisions—State Audit, County Audit, and Municipal Audit—and employs approximately 300 people. Each division is administered by a director and is responsible for the audit function and addressing concerns and issues in auditing in the division. The Assistant to the Comptroller for the Department of Audit is responsible for overseeing department-wide activities and coordinating with the directors in carrying out the goals and objectives of each of the three audit divisions.

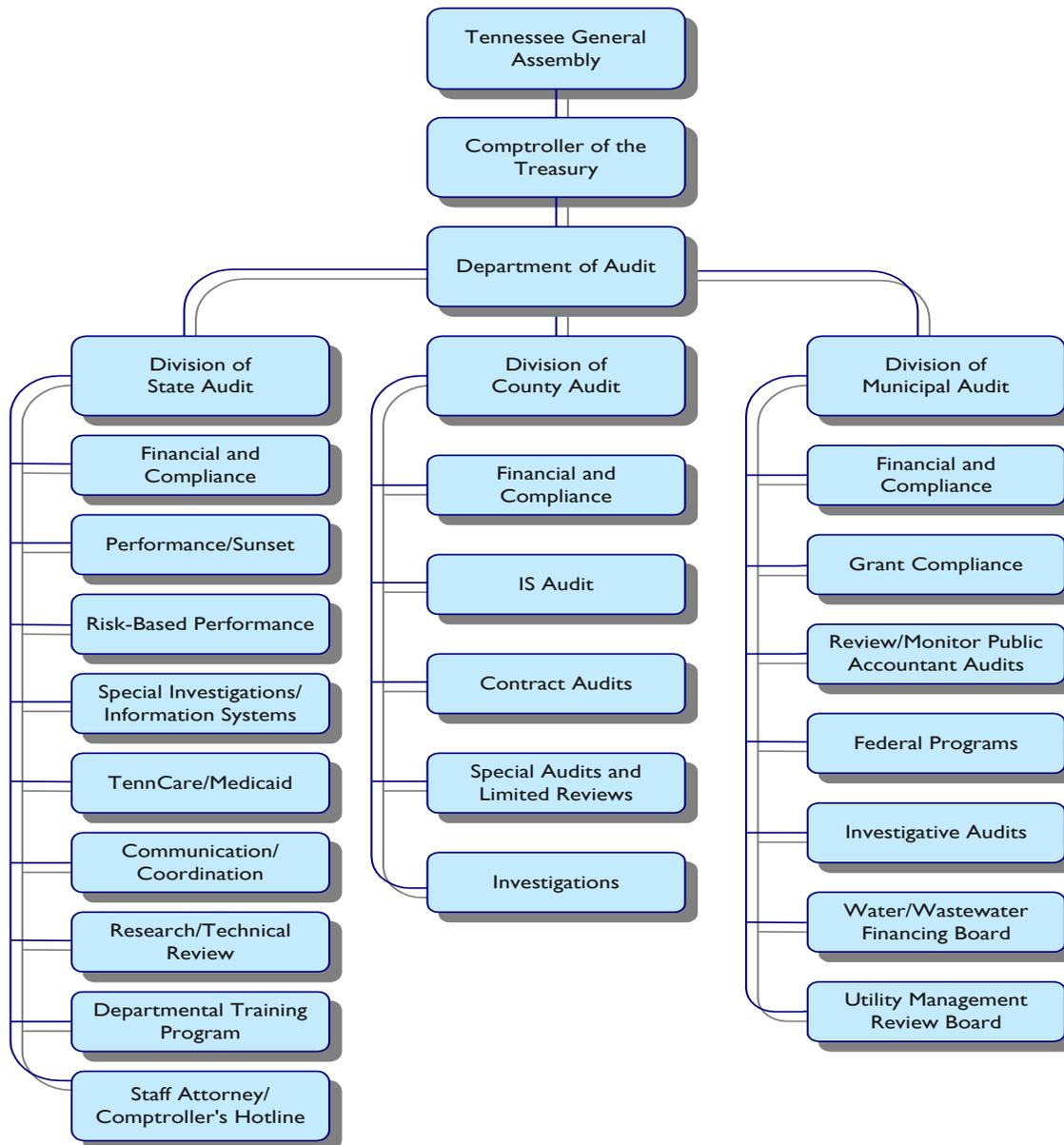
The Department of Audit is a post-audit agency. As such, it audits an entity's basic financial statements; an entity's compliance with applicable statutes, grant agreements, rules, and regulations; and/or its past record of efficiency and effectiveness at the end of a fiscal period.

Because independence is so important in a post-audit agency, the Department of Audit is in the legislative branch of state government. The department is accountable to the General Assembly and provides information to assist the legislature in overseeing the use of public funds and the efficient operation of government.

The basic purpose of post-audits is to identify and report material errors and recommend improvements. Pre-audits, in contrast, are performed by an entity's employees to prevent fraud and errors, detect problems, and suggest improvements. The most important distinction between the two is that post-audits are independent of the audited entity. In this respect, a post-audit agency in government is comparable to an independent certified public accounting firm in the private or business sector.

For additional information on the Department of Audit and the Comptroller, go to [www.comptroller1.state.tn.us](http://www.comptroller1.state.tn.us).

## Department of Audit



### Auditing Standards

The Department of Audit performs its audits in accordance with auditing standards generally accepted in the United States of America and generally accepted government auditing standards as set forth by the Comptroller General of the United States in *Government Auditing Standards* (Yellow Book).

These standards apply to financial and performance audits and attestation engagements. The Yellow Book incorporates auditing standards generally accepted in

the United States of America for field work and reporting and attestation standards promulgated by the American Institute of Certified Public Accountants.

The Department of Audit conducts its Single Audit in accordance with the Single Audit Act as amended by the 1996 Single Audit Act amendments and Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

## Peer Review

To comply with Section 8-4-102, *Tennessee Code Annotated*, the Speakers direct the Department of Audit to undergo a quality assessment review under the auspices of the National State Auditors Association. The most recent was performed in July 2010 by certified public accountants and other federal and state government professionals. The purpose of the review was to ensure that the department is following auditing standards generally accepted in the United States of America and standards contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

The peer review for the year ended June 30, 2010, rendered an unqualified opinion on the department's system of quality control. In the opinion of the quality assessment team, "the system of quality control of the State of Tennessee Comptroller of the Treasury, Department of Audit in effect for the period of July 1, 2009, through June 30, 2010, has been suitably designed and was complied with during the period to provide reasonable assurance of conforming with applicable auditing standards." The next review is scheduled for August 2012.

## The American Recovery and Reinvestment Act

The \$787 billion American Recovery and Reinvestment Act of 2009 (ARRA) supplements 60 existing federal programs and provides funding for approximately 109 new federal programs. The State of Tennessee will receive approximately \$6 billion for fiscal years 2009-2012. The Office of the Comptroller of the Treasury, Department of Audit, has been largely responsible for auditing these dollars via the Single Audit process, which will ensure that these public funds have been expended responsibly and in a transparent manner to meet the objectives of ARRA: job creation, economic recovery, and other purposes.

ARRA calls for rigorous and continuous oversight and accountability, and the Comptroller of the Treasury is committed to meeting that responsibility. At a base level, the Department of Audit will be monitoring ARRA funds as part of Tennessee's statewide Single Audit by the [Division of State Audit](#). In addition, the Comptroller has called for increased expenditure reviews and real-time reviews of internal control related to ARRA compliance. The Department of Audit will communicate, via interim reporting, significant deficiencies, material weaknesses, and other noncompliance to those charged with governance to encourage prompt corrective action.

The Comptroller of the Treasury's Office will report on the state's ability to comply with federal requirements—both by department and by major federal program. The number and type of federal programs audited as part of the Single Audit are formula driven as stipulated by the federal Office of Management and Budget (OMB). In fiscal year ending June 30, 2011, the Division of State Audit audited 25 major federal programs because of the funds expended.

The [Division of County Audit](#) has played a leading role in implementing ARRA for county governments in the State of Tennessee. All county governments in the State of

Tennessee have received ARRA grants. In terms of dollar amounts awarded, ARRA grants reached their peak for fiscal years ended June 30, 2010, and 2011. OMB has categorized ARRA grants as higher risk for the purpose of major program determination. County Audit has found it necessary to audit many more federal grants than in years past because the new ARRA grants meet OMB's criteria as major programs.

The [Division of Municipal Audit](#) released an update of the *Internal Control and Compliance Manual for Tennessee Municipalities* shortly following the passage of ARRA. The manual requires each municipality to perform a risk assessment of the municipality as a whole and design and implement internal controls to address the risks identified. The manual, in conjunction with the additional ARRA specific guidelines and implementation tools posted on our website, provides significant guidance for local governments and nonprofit organizations in complying with the mandatory transparency and accountability provisions of ARRA.

In addition, the review section of the Division of Municipal Audit has structured its post audit activities to focus on ARRA requirements. Such activities are intended to ensure that noncompliance is identified, reported, and that, ultimately, corrective action is implemented on a timely basis. The investigative section of the Division of Municipal Audit will determine how to address any ARRA deficiencies that are uncovered during its investigations on a case by case basis.

Many municipal governments and nonprofit agencies in the State of Tennessee either have received or will receive ARRA grants. Please visit the state's website at <http://www.tnrecovery.gov/plans.html> for details. □



# Comptroller of the Treasury Strategic Plan Framework



## *Mission*

**To improve the quality of life for all Tennesseans  
by making government work better**

## *Purpose*

**To serve the people of Tennessee by:**

- Contributing to the protection of the public trust and promoting the public interest
- Enhancing effective public policy decisions at all levels of government
- Fulfilling operational and oversight responsibilities as may be assigned with the highest possible degree of excellence, efficiency, and effectiveness

## *Goals and Objectives*

**Assure public resources are used effectively, efficiently,  
and in compliance with applicable law**

- Exercise an oversight role of governmental entities and agencies
- Continue to evaluate the effectiveness and efficiency of resources used by each division through a performance-based operation
- Ensure the secure, efficient, and effective use of technology solutions

**Accomplish and provide continuous improvement for the statutory  
and other assigned responsibilities of the Comptroller's Office**

- Use cross-divisional teams to address office-wide themes and appropriate strategic objectives
- Continue to advance the Comptroller's Office to a performance-based operation

**Provide timely, adequate, and accurate information to decision makers at all government levels**

- Maintain a process to develop appropriate information for decision makers
- Maintain a process to provide decision makers with appropriate information concerning policy, resource use, and management
- Encourage cooperation and joint efforts among divisions

**Provide a diverse, competent, ethical and professional staff  
and maintain continual development of such staff**

- Adhere to a uniform Code of Ethics Program
- Maintain a succession plan for management
- Maintain a training program for the continual development of all staff
- Seek a healthy and safe work environment
- Review compensation issues within the Comptroller's Office on an annual basis
- Maintain a recruiting and hiring process that promotes diversity

**Provide and maintain effective communication with internal and external audiences**

- Maintain and improve a program which coordinates timely communications using the best available technology for internal and external communications
- Maintain appropriate historical information
- Inform and educate the citizens of the state, the general assembly, and other government entities about the role of the Comptroller
- Maintain a pro-active presence in professional organizations and associations

## *Core Values*

<i>Honesty and Integrity</i>	<i>Accuracy and Reliability</i>	<i>Accountability</i>
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# Division of State Audit

The Division of State Audit conducts financial and compliance audits, performance audits, and investigations. It also performs special studies to provide the General Assembly, the Governor, and the citizens of Tennessee with objective information about the state's financial condition and the performance of the state's agencies and programs. This division thus aids the legislature in ensuring that state government is accountable to the citizens of Tennessee. In fulfilling this audit function, the division issued 64 reports during the year ended June 30, 2011; an additional 87 audits and special investigations were in progress at June 30, 2011.

This division includes six sections: Financial and Compliance, Performance (Sunset), Risk-Based Performance, TennCare, Special Investigations, and Information Systems. Highlights of work from July 1, 2010, through June 30, 2011, are presented. Complete reports are available at [www.comptroller1.state.tn.us/sa/AuditReportCategories.asp](http://www.comptroller1.state.tn.us/sa/AuditReportCategories.asp).

In addition to auditing, the division reviews and comments on due process documents from professional organizations and conducts technical research and training. The division also assists the Comptroller in the formulation of state policy and regulations, either directly by consulting with representatives of state agencies or indirectly by submitting comments about proposed policies and procedures.

## Financial and Compliance

The Financial and Compliance section conducts financial and compliance audits of state departments, agencies, and institutions.

A major endeavor of the Financial and Compliance section was the Single Audit of the State of Tennessee for the year ended June 30, 2010, conducted in accordance with *Office of Management and Budget (OMB) Circular A-133*. The *Single Audit Report* reflected federal awards of over \$16 billion.

We noted instances of noncompliance that resulted in qualified opinions on compliance for 4 of the state's 25 major federal programs. In addition, we noted other instances of noncompliance that meet the reporting criteria contained in OMB Circular A-133. We also noted material weaknesses and significant deficiencies in internal control over compliance with requirements related to federal programs.

As a result of testing the state's compliance with the requirements of laws, regulations, contracts, and grant agreements applicable to each major federal program, costs of \$11,316,397 were questioned. We noted two deficiencies that we considered to be material weaknesses in internal control over financial reporting. We noted no instances of noncompliance that we considered material to the state's basic financial statements.

The Single Audit included an audit of the state's basic financial statements. This audit resulted in an unqualified opinion on the basic financial statements of the State of Tennessee for the year ended June 30, 2010.

The audit also determined that the Schedule of Expenditures of Federal Awards was fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

In addition to the *Single Audit Report*, separate audit reports were issued on many agencies and institutions of state government including the Department of the Treasury, the Tennessee Consolidated Retirement System, state universities, the Tennessee State School Bond Authority, the Tennessee Local Development Authority, the Tennessee State Veterans' Homes Board, and the Tennessee Housing Development Agency.

The separate audits of the departments, agencies, and institutions are not meant to serve as organization-wide audits as described in the Single Audit Act as amended in 1996 and OMB Circular A-133. Some, however, serve as segments of the organization-wide audit of the State of Tennessee; therefore, they include the necessary tests for compliance with applicable laws, regulations, contracts, and grant agreements and the required consideration of the internal control.

## Audit Process

Financial and compliance audits are conducted in accordance with auditing standards generally accepted in the United States of America and generally accepted government auditing standards issued by the United States Comptroller General. The objectives of financial and compliance audits are

- to consider the entity's internal control over financial reporting as a basis for designing auditing procedures to express an opinion on the financial statements;
- to determine compliance with certain provisions of laws, regulations, contracts, and grant agreements;
- to determine the fairness of the presentation of the financial statements; and
- to recommend appropriate actions to correct deficiencies.

## Results of Audits

During the year ended June 30, 2011, the division published 40 financial and compliance audit reports containing 47 audit findings and issued opinions on 46 sets of financial statements. On June 30, 2011, another 45 audits were in progress. The section released financial and compliance audit reports for the following entities:

- ◇ Austin Peay State University
- ◇ Clean Water State Revolving Fund
- ◇ Comprehensive Annual Financial Report 2009, 2010
- ◇ Department of Commerce and Insurance
- ◇ Department of State
- ◇ Department of the Treasury 2009, 2010
- ◇ East Tennessee State University
- ◇ Fiscal Review Committee
- ◇ Local Government Group Insurance Fund 2009, 2010
- ◇ Middle Tennessee State University
- ◇ Nashville State Community College
- ◇ Northeast State Technical Community College
- ◇ Pellissippi State Technical Community College
- ◇ Retiree Health Fund 2009, 2010
- ◇ Roane State Community College
- ◇ Roane State Community College Foundation
- ◇ Single Audit for the State of Tennessee 2009, 2010
- ◇ Teacher Group Insurance Fund 2009, 2010
- ◇ Tennessee Arts Commission
- ◇ Tennessee Consolidated Retirement System
- ◇ Tennessee Education Lottery Corporation
- ◇ Tennessee Housing Development Agency

- ◇ Tennessee Local Development Authority 2009, 2010
- ◇ Tennessee Residence Foundation
- ◇ Tennessee Sports Hall of Fame
- ◇ Tennessee State University
- ◇ Tennessee State University Foundation
- ◇ Tennessee Student Assistance Corporation
- ◇ Tennessee Technological University
- ◇ Tennessee State Veterans' Homes Board
- ◇ University of Memphis
- ◇ University of Tennessee
- ◇ Walters State Community College

## Special Investigations

The Special Investigations section gathers information and evidence resulting in prosecutions and recovery of funds and coordinates the efforts of other agencies in the investigation, with authority provided in part by Sections 8-4-201 through 8-4-208, *Tennessee Code Annotated*. The investigators assist local district attorneys general, Tennessee's Office of the Attorney General, the Office of the United States Attorney General, and the Tennessee Bureau of Investigation.

Investigative reviews are initiated as a result of information from the Department of Audit, individuals, other departments and agencies, or the comptroller's hot line answered by staff of the section.

For the year ended June 30, 2011, the section received a total of 209 notifications of possible fraud, waste, or abuse. At the beginning of the year, the section had 17 active cases. During the year, the section opened 5 cases and closed 8 cases, with an outstanding balance of 14 cases at year-end. Investigations were completed on matters at the state as well as local level. Matters investigated ranged from alleged embezzlement of public funds to alleged abuse of public resources. One report was released:

Review of Expenses of the Tennessee State Museum Foundation and Other Matters Involving the Foundation and the Tennessee State Museum

Investigators found that weak internal controls or ineffective management were contributing factors in most of the losses incurred as a result of fraud. When investigators find such weaknesses, they share the information with State Audit financial auditors for consideration in audits of the affected entity.

Ongoing investigations resulted in one indictment.

## Performance

A performance audit is an independent examination of the extent to which agencies and departments of state government are faithfully carrying out their programs. The audit reports assist the General Assembly and agency management by

- assessing the extent to which state agencies have fulfilled their statutory mandate and the efficiency and effectiveness of their organization and use of resources,
- developing recommendations for management or legislative action that might improve the efficiency and effectiveness of the agencies' operations, and
- providing program and financial data.

Most of the Performance Audit section's workload is directed by the Tennessee Governmental Entity Review Law, known as the Sunset Law (Section 4-29-101 et seq., *Tennessee Code Annotated*), which requires the Joint Government Operations Committee to review each entity at least once every eight years to determine whether the entity should be continued, restructured, or terminated.

Other performance audit work is based on risk assessment of state department and agency programs. The risk-based performance audit group conducts audits based on identification of risks in state-wide processes and programs and agency-specific operations and activities. During FY2011, with increased federal funding and new reporting requirements under the American Recovery and Reinvestment Act of 2009, state agencies were at greater risk of fraud, waste, abuse, and noncompliance with federal program requirements. The risk-based performance audit group performed audits of those state agencies with the greatest risks.

Audit staff focus on audits of major entities. In the year ended June 30, 2011, the Performance Audit section released the following 15 reports:

### Sunset Audit Reports

- ◇ Commission on Aging and Disability
- ◇ Department of Children's Services, Division of Juvenile Justice
- ◇ Department of Education and the State Board of Education
- ◇ Department of Finance and Administration
- ◇ Department of Human Resources and the Civil Service Commission
- ◇ Department of Safety Follow-up Report
- ◇ Department of Transportation
- ◇ Human Rights Commission
- ◇ Tennessee Community Services Agency

### Special Reports

- ◇ Department of State
- ◇ Joint Oversight Committees
- ◇ Office of Legislative Administration
- ◇ Office of the Comptroller of the Treasury
- ◇ Review of Plans and Analysis for Reducing the Use of Petroleum Products
- ◇ Study of the Feasibility of Dividing Licensure Functions Between the Department of Mental Health and Developmental Disabilities and the Department of Intellectual and Developmental Disabilities

Eighteen engagements were in process at year-end.

The Government Operations Committees held 15 public hearings on 37 entities in the year ended June 30, 2011. At these hearings, Performance Audit staff presented audit reports covering 11 entities. Another 21 entities submitted written responses to staff-prepared questions based on the entities' statutory authority and responsibility. Additionally, Investigative staff presented information pertaining to one entity, and seven entities provided information pertaining to self-sufficiency issues or provided updates pertaining to activities of interest to the committees.

### Audit Process

Performance audits are conducted in accordance with *Government Auditing Standards* issued by the United States Comptroller General and move through six phases: planning, fieldwork, report writing, agency comments, report publication, and presentation at a legislative hearing. Performance audits include the following:

- Review of relevant laws, cases, Attorney General's opinions, executive orders, rules, and regulations.
- Review of the agency's procedures, plans, and records.
- Interviews with staff of the agency and related agencies.
- Observation of the agency's operations and activities.
- Analysis of the agency's revenue and expenditure data, program data, performance, and results.
- Review of comparative data from other states.
- Surveys of individuals, agencies, and organizations served or affected by the agency.
- Tests for compliance with legal requirements.
- Evaluation of the extent to which the agency achieved desired results at the lowest reasonable cost.
- Legislative or administrative recommendations for accomplishing the agency's legislative mandate.

## TennCare

The TennCare section of the Division of State Audit, under an agreement with the Department of Finance and Administration, performs certain audit and rate-setting functions for the state's TennCare program. A staff of 22 professional auditors performs the following functions:

- Reimbursable rate computation and examinations for nursing homes and Intermediate Care Mental Retardation facilities participating in the Medicaid Program.
- Computing of reimbursement settlements and prospective rates for Federally Qualified Health Centers and Rural Health Clinics as required by the Benefits Improvement and Protection Act of 2000.
- Cost settlements for state-operated Development Centers serving mentally retarded recipients.
- Agreed-upon procedures engagements performed to compute the Certified Public Expenditures (CPE), or unreimbursed TennCare costs, for which public hospitals may receive additional funding.

## Information Systems

The Information Systems (IS) section provides three basic services: data retrieval, IS systems review, and computer forensic analysis.

To provide information for audit fieldwork, the data retrieval staff write computer programs to provide information from the state's centralized accounting system, individual agency service delivery systems, and college and university transaction files.

The IS review staff are responsible for obtaining and documenting an understanding of internal control in the computerized accounting and management information systems of entities undergoing audits by other sections of the division. Three audits were in progress at June 30, 2011.

The IS section provides services in the area of computer forensic analysis. Evidence of fraud and abuse may be found on subjects' computers, and the IS section works in support of the special investigations section to acquire, identify, and analyze this evidence. The section utilizes specialized software and hardware to recover evidence of official misconduct by state employees and in support of civil or criminal action against persons or entities engaging in illegal activities resulting in damages to the state.

- Provide financial and budgeting support to the Bureau from nursing home paid claims extracts.
- Examinations of TennCare Managed Care Contractors (MCCs) contracting with the state to provide medical services under the program, performed jointly with the Department of Commerce and Insurance.

## Examinations of Nursing Facilities

In the fiscal year ended June 30, 2011, the TennCare section completed eight examinations of the following nursing facilities:

- ◇ Allenbrooke Nursing and Rehabilitation Center
- ◇ The Bridge at Rockwood
- ◇ Poplar Point Health and Rehabilitation
- ◇ Briarwood Community Living Center
- ◇ Graceland Nursing Center
- ◇ Laurelbrook Sanitarium and School
- ◇ Newport Health and Rehabilitation Center
- ◇ Norris Health and Rehabilitation Center

Seven examinations were in progress at year-end.

## Examinations of TennCare MCCs

In the fiscal year ended June 30, 2011, the TennCare section assisted the Department of Commerce and Insurance in two Managed Care Contractor (MCC) examinations. The summary of findings included financial, claims processing, and compliance deficiencies.

## Special Projects – Grier Consent Decree

The state, legislature, or federal government often requests that the Division of State Audit work on special TennCare projects. In one such project, the state, under a consent decree with the federal court, has agreed to comply with requirements with respect to TennCare enrollee grievances and appeals. The TennCare managed care contractors and providers are also subject to the decree, so it has widespread implications.

The agreement, commonly referred to as the "Grier Consent Decree," became effective November 1, 2000. The decree requires the state to enter into an agreement with the Comptroller's Office to monitor compliance and to report quarterly. Reports through the end of 2010 have been completed, and reports for 2011 are in progress. □



# Division of County Audit

The Department of Audit, through the Division of County Audit, is responsible for the annual audits of all 95 counties in the state. The division may conduct the audit of a county or accept an audit prepared by a certified public accountant provided the audit meets minimum standards for county audits established by the Comptroller of the Treasury. However, the Division of County Audit is required to prepare an audit in each county at least once every five years or to participate with, or monitor the audit with, the certified public accountant.

## Financial and Compliance

The division presently conducts audits in 89 counties. These audits are assigned to teams that audit the various offices and/or departments and entities of county government. The audit staff is divided into four geographical areas: East, Mideast, Middle, and West. Each area is under the supervision of an audit manager who is responsible for audit planning and supervision.

## The Audit Process

The Division of County Audit performs the following general procedures as part of the financial and compliance audit process:

- Evaluates the entity's existing internal controls in the appropriate areas of operation.
- Confirms the accountability for receipts by examining, for example, tax rolls, state and federal revenue data, and letters of inquiry.
- Determines the appropriateness of disbursements by examining budget authorization, paid invoice files, purchasing files, payroll records, and other financial records.
- Determines the authorization for transactions by reviewing the minutes of meetings of county commissions, school boards, highway commissions, and various committees such as budget and finance, and purchasing.
- Determines compliance with federal regulations and state and local laws.
- Obtains management's representations with respect to the financial statements, as well as the supporting accounting data, and other items of disclosure.

- Evaluates financial statement presentation to determine conformity with accounting principles generally accepted in the United States of America.
- Evaluates the validity of all evidence obtained throughout the audit process to formulate an opinion on the financial statements.

## Scope of Activity

### Post-Audit of County Governments

The Division of County Audit conducted audits in 89 of the state's 95 counties for the 2009-10 audit year. A minimum of ten offices or departments in each county was audited:

1. County Trustee
2. County Mayor
3. Department of Education
4. Department of Highways
5. County Clerk
6. Circuit Court Clerk
7. General Sessions Court Clerk
8. Chancery Court Clerk and Master
9. Register
10. Sheriff

The audits of all offices were for the fiscal year ended June 30, 2010. The audit field work in each county is conducted by an audit team. The size of the team is determined by the complexity of the assignment. Approximately ten weeks of field work are required, including audit review and supervision by an auditor 4 and/or audit manager. The draft audit reports are reviewed in the Nashville office and released. The division also prepares audits of two special school districts and performs special audits and reviews as requested or as deemed necessary.

## Results of Audits

### Financial and Compliance Audits

Audits of financial transactions for the fiscal year ended June 30, 2010, conducted by the Division of County Audit disclosed cash shortages in the following offices or funds:

The audits conducted or reviewed by this division disclosed fund deficits totaling \$130,752,591 in 54 governmental fund accounts in 34 counties. Audits also reflected net asset deficits totaling \$53,188,852 in 14 enterprise funds and 7 internal service fund accounts in 13 counties. Details of the latest cash shortages report are available on the Comptroller's website at [www.tn.gov/comptroller/](http://www.tn.gov/comptroller/).

### Information System Reviews

Most county government offices and departments in Tennessee have automated all or a portion of their daily operations. The information system (IS) review section is responsible for evaluating those computer-based accounting and information systems to determine whether an entity's existing procedures and controls provide adequate assurance of data accuracy and financial and operating statement reliability. An assistant director supervises this section's IS audit manager and seven IS auditors, who are assigned to different areas of the state.

General and application controls of a county's computer hardware and computerized accounting and information systems are evaluated. Findings resulting from this evaluation are discussed with the appropriate officials and included in the county's annual financial report.

### Scope of Activity

#### Information System Reviews

As required by the division's annual audit plan, information system related controls were evaluated in 89 counties and two special school districts during the year ending June 30, 2011.

### Contract Audits

For six counties, certified public accountants perform the financial and compliance audits. The division monitors these audits in accordance with a four-year monitoring plan, which includes a review of working papers prepared by certified public accountants.

The division also approves the contracts of certified public accountants and reviews their audit reports and working

papers. The objective of this review is to ensure that in addition to the standards prescribed by the American Institute of Certified Public Accountants and Government Auditing Standards issued by the United States Comptroller General, certain standards prescribed by the Comptroller of the Treasury have been followed.

### Scope of Activity

#### Monitoring and Review of Contract Audits

The division will monitor audits of six county governments during the next four years. The audit of Hamilton County was monitored for the year ended June 30, 2010, and the audits of Washington and McMinn counties will be monitored for the year ended June 30, 2011.

The division reviewed 287 audit reports for the year ended June 30, 2010, submitted by certified public accountants for audits of county governments, authorities, boards, commissions, agencies, and special school districts. The division anticipates it will review 287 such reports for the year ended June 30, 2011.



## Investigations

A County Audit investigations team performs investigations on reported instances of fraud, waste, and abuse. The team consists of four auditors, one based out of each of the division's regional offices. An investigations manager sets priorities, allocates resources, and coordinates investigations with area audit managers. The investigative auditors' primary responsibility is to perform investigations in their geographic area resulting from hot line calls, fraud reporting forms, anonymous tips, significant cash shortages discovered during the routine audit process, and other reported instances of fraud, waste, and abuse. Results of investigations, such as findings and any impact on county financial statements, will be reported in the annual county audit reports. On occasion, a separate investigative report may be issued.

In most cases, investigative auditors discovered weak internal controls or ineffective management that created an environment where fraud could occur and go undetected. During the fiscal year ended June 30, 2011, the division released 10 special investigative reports revealing a loss of county funds to fraud totaling \$524,827.66. The following special reports were released in the fiscal year June 30, 2011:

- ◆ Williamson County Animal Control Department
- ◆ Hickman County Clerk
- ◆ Marion County Election Office
- ◆ Lake County Mayor's Office
- ◆ Tipton County School Department
- ◆ Fayette County School Department
- ◆ Cumberland County Election Office
- ◆ Halletown Volunteer Fire Department
- ◆ Morgan County Clerk
- ◆ Franklin County Probation Office

## Other Services

### Technical Assistance

In addition to the basic audit function and the monitoring and review of audits by certified public accountants, the division provides other services. These services include providing information and assistance to facilitate implementation of new auditing and accounting standards; submission of federal program data to the federal clearing house on behalf of county governments; requesting technical data for pension and other postemployment benefits note disclosures from the State

of Tennessee; maintenance of the uniform chart of accounts used by county governments; and participation in the review of telephone calls made to the Comptroller's Fraud Hotline. The division also provides, upon request, assistance to counties in resolving current problems with financial administration, as well as answering questions on various local governmental matters. The division provides fiscal reviews of new legislation related to county governments and works closely with the state legislature with regard to the passage of new statutes for county governments.

### Reviews of Funds Administered by District Attorneys General

During 2011, the division conducted reviews of District Attorney General Funds, Judicial District Drug Task Force Funds, and other funds the district attorneys general administer in the state's 31 judicial districts. Each review covered the period July 1, 2009, through June 30, 2010. The scope of each review was limited to the transactions of the individual funds and did not include the overall operation of the district attorneys' offices.

### Reviews of County Correctional Incentive Program (CCIP)

*Tennessee Code Annotated*, Title 41, Chapter 8, referred to as the County Correctional Incentive Act, provides counties financial incentives to house nondangerous felony offenders at local correctional facilities. The purpose of the program is to mutually benefit state and county governments by helping to alleviate overcrowding in state correctional facilities and reduce high operating costs, and to assist counties in upgrading local correctional facilities and programs. Counties participating in the program may be reimbursed at either a minimum statutory daily rate or a rate based on a county's "reasonable allowable cost" to house convicted felons.

The Division of County Audit conducts reviews of various counties participating in the CCIP. The objectives of the reviews were 1) to determine if prisoners were properly listed on the State Prisoner Reports, 2) to determine if inmates were accurately reported on the Correction Facility Summary Reports, and 3) to recommend appropriate actions to correct any deficiencies.

Reviews were conducted in 24 detention facilities for the year ended June 30, 2009. As a result of the reviews, it was determined that the state had overpaid \$54,849 for six facilities and underpaid \$124,204 for three facilities. □



# Division of Municipal Audit

The Division of Municipal Audit ensures that annual audits, required by state statute, are performed for all Tennessee municipalities, public school activity and noncentralized cafeteria funds, utility districts, housing authorities, charter schools, and certain nonprofit agencies receiving grants from the State of Tennessee. Also, as required by state statute, the division ensures that an agreed-upon procedures audit is performed for certain daycare providers receiving subsidy payments through the State of Tennessee. In addition, the division investigates allegations of misconduct, fraud, waste, and abuse in these entities.

## Audit Review Process

Local governmental units (other than counties) and nonprofit agencies contract with independent certified public accountants to perform annual audits of Tennessee's 344 municipalities, 106 city-related entities, 78 quasi governmental entities, 47 quasi nonprofit entities, 183 utility districts, 144 public school activity and noncentralized cafeteria funds, 32 charter schools, 85 housing authorities, 3 housing authority related entities, and 229 nonprofit agencies. The entities use standard contracts, prepared by the Comptroller of the Treasury that must be approved by the Comptroller's designee in the Division of Municipal Audit before audit work begins. Audits must be performed in accordance with generally accepted government auditing standards issued by the United States Comptroller General or agreed-upon procedures prescribed by the American Institute of Certified Public Accountants and certain other requirements prescribed by the Comptroller of the Treasury. In addition, the auditor must comply with other federal and state provisions.

The Division of Municipal Audit reviews each audit report to verify that it adheres to applicable requirements. If a local governmental unit or nonprofit agency fails or refuses to have an audit, the Comptroller may direct the Division of Municipal Audit, or may appoint a certified public accountant, to perform the audit. The division evaluates the audit working papers of certified public accounting firms that audit local, governmental, and nonprofit entities. If the firm's audit working papers are deemed substandard, the Comptroller of the Treasury takes appropriate action, which might include referral to the State Board of Accountancy. The division is responsible for tracking 1,382 nonprofit organizations that have received grants from the State of Tennessee; some are required to have an audit of their entire organization. These audits are conducted by certified public accounting firms, which contract with the division.

## Wastewater and Utility Districts

Sections 68-221-1010 and 7-82-401g(1), *Tennessee Code Annotated*, require the Comptroller to refer financially distressed municipal wastewater and public utility districts to the state's Water/Wastewater Financing Board or the Utility Management Review Board. After reviewing the audit reports, the Division of Municipal Audit refers financially distressed facilities to the appropriate board. The board then reviews the current financial condition of the facility and its proposed plan for eliminating its financially distressed condition. If the board finds the facility's plan unacceptable, the board will recommend an alternate course of action.

During the year ended June 30, 2011, 107 water/wastewater facilities were referred to the Water/Wastewater Financing Board, and 55 utility districts were referred to the Utility Management Review Board. (The increase in referrals was due to water loss referrals required by *Tennessee Code Annotated*.) As a result, several utility districts and municipal water and/or sewer systems are now operating or are on their way to operating on a financially sound basis.

## Investigative Audits

The division investigates allegations of misconduct, fraud, waste, and abuse in specified local governments and other publicly funded entities. Investigative audits are performed as a result of allegations received through the Department of Audit's toll-free hotline, routine audit reviews, information received from certified public accountants, other state agencies, concerned citizens and/or officials, and requests received from local district attorneys general, the State Attorney General's Office, the FBI, and other prosecutorial and law enforcement agencies. Upon completion of each investigation, the Comptroller issues a report or letter presenting documented

occurrences of improper activity and recommending corrective action. The report is forwarded to the State Attorney General and the local district attorney general for any legal action deemed necessary.

The division also conducts investigative audits that include a thorough review of internal control and compliance with applicable laws. Municipalities are required by statute to maintain their records, at a minimum level, in accordance with the *Internal Control and Compliance Manual for Tennessee Municipalities*, prescribed by the Comptroller of the Treasury. Utility districts are required by state statute to follow the *Uniform Accounting Manual for Tennessee Utility Districts*, compiled by the Division of Municipal Audit. State statute requires schools to follow the *Tennessee*

*Internal School Uniform Accounting Policy Manual*, compiled by the Tennessee Department of Education, the Department of Finance and Administration, and the Division of Municipal Audit. At the conclusion of an investigative audit, the division publishes a report that identifies internal control and compliance deficiencies and recommends corrective action. The audits point out to officials the importance of sound internal controls and compliance with applicable laws and regulations.

The division routinely provides technical assistance to local government officials and to certified public accountants. This assistance often requires detailed research of financial accounting concepts and state and federal statutes.

## Audits and Investigative Audits

For the year ended June 30, 2011, the Division of Municipal Audit performed 1,041 reviews of audit reports for specified local governments and other publicly funded entities. The division released 32 investigative audits during the year. The entities examined in the 32 investigative audits included 9 municipalities, 6 public schools, 2 nonprofit entities, 8 utility districts, 6 school support organizations, and one other entity. The majority of the investigative audits involved allegations of fraud, waste, and abuse. Most investigative audits revealed deficiencies in internal controls, absence of internal controls, or potential problem areas that created an environment conducive to fraud. During the 2011 fiscal year, investigative audits revealed losses of at least \$608,898 due to fraud. In total, approximately 13 defendants' cases were disposed of in fiscal year 2011. Approximately 45 criminal indictments were dealt with altogether. In all, 12 entity-victims throughout the state recovered \$377,043 (including stolen amounts and audit costs) as a result of the investigation and subsequent prosecution of the criminal cases.

The Division of Municipal Audit released the following investigative reports during the year ended June 30, 2010:

- ◇ PALS-W.A. Wright Elementary School PTO – Wilson County Schools
- ◇ Gateway Elementary School Parent-Teacher Association
- ◇ Unicoi County Band Boosters Association
- ◇ Shelby County Register of Deeds
- ◇ Lake Road Elementary PTO – Obion County Schools
- ◇ Vonore Police Department
- ◇ Trenton Police Department
- ◇ Monterey Police Department
- ◇ City of Ripley – Gas, Water and Wastewater
- ◇ Powell-Clinch Utility District
- ◇ Bon Lin Elementary School and Rivercrest Elementary School Cafeteria Funds – Shelby County Schools
- ◇ Powell-Clinch Utility District – Costa Rica Builders Trip
- ◇ Sevier County Utility District – Costa Rica Builders Trip
- ◇ Hawkins County Utility District – Costa Rica Builders Trip
- ◇ Oak Ridge Utility District – Costa Rica Builders Trip
- ◇ Jefferson-Cocke County Utility District – Costa Rica Builders Trip
- ◇ City of Parsons
- ◇ Haywood Elementary School PTO – Metro Nashville Public Schools
- ◇ Heritage High School – Blount County Schools
- ◇ City of Smithville
- ◇ Coal Miners Museum of the Cumberlands Grant (Lake City)
- ◇ Eagles Landing Golf Course – City of Sevierville
- ◇ Town of Baxter – Police Department (Evidence)
- ◇ Clarksville/Montgomery County Community Action Agency
- ◇ Mt. Pisgah Middle School PTA – Shelby County Schools
- ◇ Sevier County Utility District
- ◇ Trezevant High School – Memphis City Schools
- ◇ City of Portland
- ◇ Evans Elementary School – Memphis City Schools
- ◇ LaFollette Middle School – Campbell County Schools
- ◇ Jacksboro Elementary School – Campbell County Schools
- ◇ Cagle-Fredonia Utility District □



# Comptroller's Hotline

Since its inception, the hotline has received over 15,000 calls, including 1,447 calls between July 1, 2010, and June 30, 2011. Of the 1,447 calls, 466 concerned allegations of fraud, waste, or abuse. The substantive calls—those relating to fraud, waste, or abuse—concerned a wide range of entities, including municipalities, counties, state agencies and departments, and federal agencies and departments. A more detailed analysis is below. Substantive calls are investigated by the Department of Audit or referred to the appropriate state agency or program.

Of the 466 calls referred for action, responses have been received on 377, and these are considered closed. The remaining 89 continue to be considered open.

The remaining 981 calls have not been acted on because they were either repeat calls or were not relevant to the purpose of the hotline. Calls in the latter group include wrong numbers, hang-ups, general inquiries about the hotline, and requests for services provided by other agencies, such as tax assistance. Where applicable, the callers are referred to the appropriate agency or department that can provide assistance.

## Results of Hotline Calls

The following summaries are the results of hotline calls upon which corrective action was taken for the year ending June 30, 2011.

### **Commerce and Insurance – Unlicensed Auctioneer**

The caller alleged that auctions were being conducted by an unlicensed auctioneer. The allegation was found to be true. The unlicensed auctioneer was required to pay a civil penalty of \$500.

### **County Audit – County Vehicles Not Properly Tagged**

The caller alleged that certain county vehicles did not have proper tags. It was found that several county owned vehicles were not registered as governmental vehicles, causing an increase in fees paid. A finding was issued based on lack of formal policies and procedures. The county commission subsequently adopted formal policies and procedures.

### **County Audit – Purchases Not Competitively Bid**

The caller alleged that purchases were not being properly bid. It was found that the county had not solicited competitive bids on certain purchases. The finding was communicated to the county for corrective action.

### **Education – Misuse of Funds**

The caller alleged that a high school was purchasing equipment for other schools' sports programs. The review determined the purchases were not an allowable cost under the billed program. The school district used local funds to reimburse the program.

### **Environment and Conservation – Nepotism**

The caller alleged that a family member was supervising another family member. The allegation was found to be true. The matter was referred to the department of human resources to find a possible resolution.

### **Finance and Administration – E-mail and Internet Abuse**

The caller alleged that an employee was abusing state e-mail and Internet privileges. The allegation was found to be true and the employee was suspended for one day without pay.

### **General Services – Water Leaks**

The caller alleged that sinks in a state building had been leaking for over two years without being repaired, resulting in unaccounted for water loss. The allegation was found to be true, and the faucets were replaced.

### **Health – Patient Neglect (Two Cases)**

In two instances, a caller alleged that a nursing home was neglecting a patient or patients. In the first instance, the facility was cited with a deficiency. In the second instance, the resulting complaint survey revealed that the facility had not met certain Medicare and/or Medicaid Program regulatory requirements. Both facilities went under a plan of correction.

### **Human Services – Unsafe Day Care Facility (Two Cases)**

In one instance, a caller alleged that a day-care facility was unsanitary. The allegation was found to be true, and the center voluntarily suspended its license. In another instance, a caller alleged that a day-care facility was not safe. The review discovered several safety hazards and the center was issued a “Put on Notice” letter to correct the hazards.

### **Human Services – Unqualified Day Care Staff**

The caller alleged that a day-care facility was using unqualified workers. The review determined that the facility employed two staff members without high school diplomas. The workers no longer work at the facility.

### **Human Services – Food Stamp Fraud (Nine Cases)**

In eight instances, a caller alleged an individual was receiving food stamp benefits for which that individual was not eligible, and the allegation was found to be true. In five of those instances, the recipient was removed from the program and the department is seeking recovery. In two instances, the department reduced the recipient’s benefits. And in one instance where the recipient had unreported income, the individual retained a reduced benefit and the department is seeking recovery for the months in question.

In another case, a caller alleged a drug and alcohol addiction recovery center was accepting food stamp payments from clients for rent. The allegation was found to be true and the center was closed as an unlicensed center.

### **Human Services – Unprofessional Behavior**

The caller alleged that an employee was allowed to bring a dog to work on occasion. The allegation was found to be true, and the office was placed under a corrective action plan.



### **Safety – Unprofessional Behavior**

The caller alleged that a license testing station employee was texting rather than assisting patrons of the station. The allegation was found to be true. The employee was issued a warning, and the Branch Supervisor reviewed the policy with the entire staff.

### **Transportation – Smoking in Government Vehicle**

The caller alleged that a transportation service employee was smoking in a government vehicle. The allegation was found to be true. The driver was advised that failure to comply with smoking policies would result in immediate termination.

### **Transportation – Unprofessional Behavior**

The caller alleged that a transportation service employee was harassing her. As a result of the review, the employee received customer service and policy and procedure training. The employee was reassigned to no longer transport the caller.

### **Transportation – Wasteful Use of State Vehicle**

The caller alleged that an employee using a government vehicle was driving out of the way to pick up another employee. The allegation was found to be true. Both employees were required to stop. □

**Comptroller's Fraud, Waste, and Abuse Hotline  
(800) 232-5454**

**Analysis of Substantive Hotline Calls**  
**Fiscal Year Ended June 30, 2011**

<b>Reviewing Agency</b>	<b>Calls</b>	<b>Closed</b>	<b>Open</b>
<u>Local Government</u>			
Municipal Audit	45	42	3
Metropolitan Development and Housing	1	1	0
South Pittsburg Housing	1	1	0
<u>County Government</u>			
County Audit	55	46	9
<u>State Government</u>			
Agriculture	4	4	0
Alcoholic Beverage Commission	1	1	0
Board of Probation and Parole	6	6	0
Board of Regents	6	4	2
Children's Services	15	15	0
Commerce and Insurance	2	2	0
Comptroller-Property Assessments	1	0	1
Correction	11	10	1
Corrections Institute	1	1	0
Education	2	2	0
Environment and Conservation	4	4	0
Finance and Administration	5	5	0
General Services	9	8	1
Health	48	45	3
Human Resources	1	1	0
Human Services	92	89	3
Intellectual and Developmental Disabilities	9	3	6
Labor	24	21	3
Mental Health	27	26	1
Revenue	3	3	0
Safety	23	18	5
State Audit	25	20	5
TennCare	3	2	1
Tennessee Bureau of Investigation	3	0	3
Tennessee Higher Education Commission	1	1	0
Transportation	29	28	1
University of Tennessee	3	1	2
<u>Federal Government</u>			
Health and Human Services	1	0	1
Housing and Urban Development	4	2	2
Internal Revenue Service	1	1	0
<b>Total</b>	<b>466</b>	<b>413</b>	<b>53</b>



# About the Department of Audit

## Department of Audit Staff

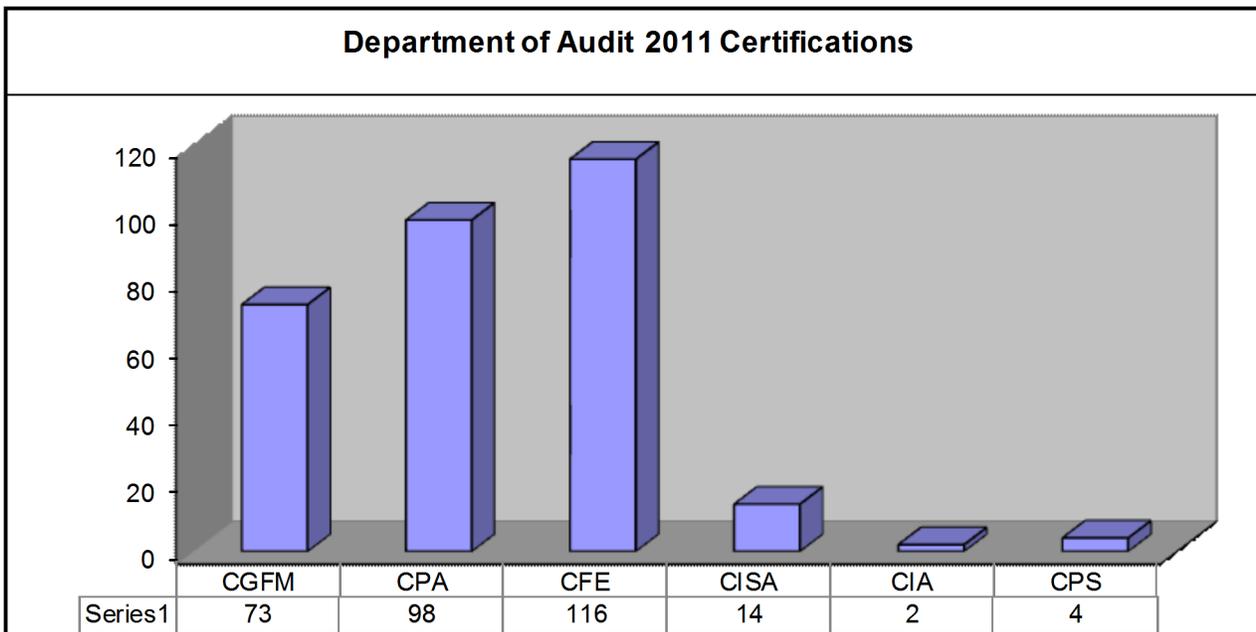
The department's professional staff perform a wide variety of audit work requiring different types of training and experience. Therefore, members of the staff have degrees in fields such as accounting, public administration, information systems, law, political science, criminal justice, education, and nursing. More than 60 of the professional staff have advanced degrees. The department encourages its employees to pursue professional certifications such as Certified Public Accountant, Certified Information Systems Auditor, Certified Fraud Examiner, and Certified Government Financial Manager.

As of June 30, 2011, more than 200 employees of the department had received one or more professional

certifications. This range of experience gives a broad perspective to the department's audit work.

The Department of Audit ensures its auditors receive the required continuing professional education to meet certification standards and Government Auditing Standards. Auditors participate in the department's in-house training program as course developers, presenters, and participants. Over 13,000 hours of training were completed during the fiscal year ended June 30, 2011.

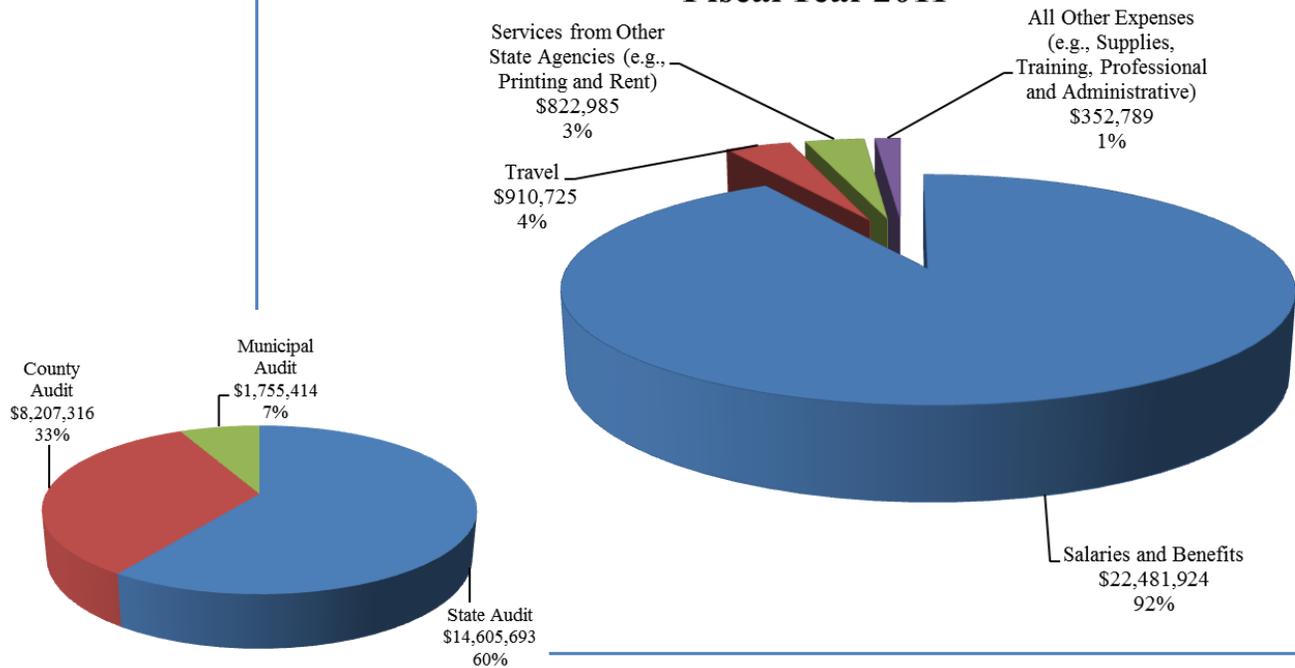
The Department of Audit fully supports its staff's active participation in local and national professional organizations, recognizing that these organizations contribute to the staff's continued growth. □



Certified Government Financial Manager (CGFM), Certified Public Accountant (CPA), Certified Fraud Examiner (CFE), Certified Information Systems Auditor (CISA), Certified Internal Auditor (CIA), and Certified Professional Secretary (CPS).

For information on the National State Auditors Association, go to  
[www.nasact.org](http://www.nasact.org).

## Department of Audit Expenditures Fiscal Year 2011



### Contact Information

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(615) 741-2501

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For additional information on the Department of Audit and the Comptroller, go to  
[www.comptroller1.state.tn.us](http://www.comptroller1.state.tn.us).