

State of Arizona
Department of Economic Security
Management Letter
Year Ended June 30, 2001



STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

DEBRA K. DAVENPORT, CPA
AUDITOR GENERAL

WILLIAM THOMSON
DEPUTY AUDITOR GENERAL

June 3, 2002

John L. Clayton, Director
State of Arizona
Department of Economic Security
1717 West Jefferson Street
Phoenix, AZ 85007

Subject: Management Letter

Dear Mr. Clayton:

In planning and conducting our financial statement audit of the Department of Economic Security and our single audit of the State of Arizona for the year ended June 30, 2001, we performed the following as required by *Government Auditing Standards* (GAS) and Office of Management and Budget (OMB) Circular A-133:

- Considered the Department's internal controls over financial reporting,
- Tested its internal controls over major federal programs, and
- Tested its compliance with laws and regulations that could have a direct and material effect on the Department's financial statements or the State's financial statements and major federal programs.

All audit findings that are required to be reported by GAS and OMB Circular A-133 have been included in the State of Arizona's Single Audit Reporting Package for the year ended June 30, 2001, and have been communicated to your staff. In addition, our audit disclosed internal control weaknesses and instances of noncompliance with laws and regulations that do not meet the reporting criteria. Management should correct these deficiencies to ensure that it fulfills its responsibility to establish and maintain adequate internal controls and comply with laws and regulations. Our recommendations are described in the accompanying summary.

This letter is intended solely for the information of the Department of Economic Security and is not intended to be and should not be used by anyone other than the specified party. However, this letter is a matter of public record and its distribution is not limited.

Should you have any questions concerning its contents, please let us know.

Sincerely,

Dennis L. Mattheisen, CPA
Financial Audit Director

Attachment

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The Arizona Industries for the Blind should improve its controls over its accounting records and assets

The Arizona Industries for the Blind (AIB) provides employment and rehabilitation for the blind. The AIB is responsible for maintaining its own accounting records and preparing its own financial statements. However, AIB lacked adequate internal controls over its accounting records and assets. Consequently, AIB could not ensure that its records or reports were accurate and fixed assets were safeguarded. The following deficiencies illustrate this lack of control.

- One employee was responsible for preparing, approving, and recording manual journal entries, transfers, and the correction of errors. This employee was also an authorized signer for all bank accounts.
- Documentation supporting three disbursements could not be located.
- The invoice number or amount for four accounts payable and one account receivable was incorrectly posted to the accounts payable or receivable aging reports.
- Depreciation expense was calculated incorrectly for numerous capital assets.
- The unit cost for six items recorded on the inventory listing was incorrect.
- A capital asset recorded on the assets listing could not be located.
- Two capital assets located on the AIB premises were not included on the assets listing.
- Six capital assets lacked a property control tag.

A finding similar to this one was reported previously.

The AIB should improve its existing controls over its accounting records and assets. Specifically, the AIB should:

*Recommended procedures for
controls over accounting
records and assets*

- ✓ Separate accounting responsibilities among its employees to ensure that no one person can sign checks as well as prepare, approve, and modify the records of financial transactions.
- ✓ Retain documentation that supports expenditures and complies with the State's record retention policy.
- ✓ Report accounts receivable and payable transactions accurately on its subsidiary systems.
- ✓ Calculate depreciation expense properly.
- ✓ Value its inventory items at actual cost.
- ✓ Record all assets valued over \$5,000 accurately on its assets listing.
- ✓ Control all capital assets with a property control tag.

The Division of Developmental Disabilities should properly reconcile its fiduciary accounts

The Division of Developmental Disabilities has six regional offices that administer the financial activity for individuals with developmental disabilities who are unable to handle their own finances. Each regional office maintains the financial activity records for disabled individuals on its personal computer. Each regional office also maintains a fiduciary bank account for depositing social security, Arizona Long-Term Care System, and other benefit cash receipts and issuing checks for disabled individuals' expenses.

In December 1999, the Division changed the software on its personal computer and did not provide adequate training to its employees on the new system. Subsequently, several regional offices incorrectly recorded the financial activity onto the new system and were unable to reconcile their accounting records to the banks' statements.

The Division should immediately correct the erroneous financial information recorded on the new system, then reconcile the accounting records to the bank statements. Performing proper monthly reconciliations will help ensure that accurate and complete financial information is maintained for each of its disabled clients.

The Department needs to improve its controls over fixed assets to ensure that they are safeguarded and its listing is accurate

The Department cannot ensure that it is adequately safeguarding its assets unless it has an accurate listing of those assets. However, the Department lacked controls to ensure that fixed assets were properly tagged and accurately recorded in its fixed assets control system. As a result, the following errors occurred:

- Some capital equipment items did not have a property control tag.
- Several fixed assets included on the listing could not be located.
- One asset was recorded on the fixed assets listing twice.
- Numerous assets recorded on the system had an incorrect property control tag number, model number, serial number, or location recorded.
- Several assets were recorded on the fixed assets listing at an estimated value; however, this estimated value exceeded the actual value by \$24,296.
- The disposal forms for deleted assets were incomplete and contained numerous errors. Specifically, the property description, manufacturer's serial number, property tag number, acquisition date, funding source, and reporting categories were excluded from the disposal forms. As a result, assets could have been incorrectly deleted from the listing.

A finding similar to this one was reported previously.

*Recommendations for
safeguarding fixed assets*

To help ensure the integrity and accuracy of the information provided by the fixed assets control system, the Department should follow internal control policies and procedures outlined in the *State of Arizona Accounting Manual*, Section G. Specifically, the Department should issue each asset a property control number and record the number, model number, serial number, location, and actual cost on the fixed assets control system. Further, the Department should properly report all required information on disposal forms.

The Department should protect its information system from damage and equipment failure

The Department's disaster recovery plan for its financial management control systems had not been updated or tested since 1988. In addition, the Department kept the plan with its computer system. Further, the Department's plan did not include a list of employees assigned to disaster recovery teams or their emergency phone numbers. Lack of an updated and tested disaster recovery plan exposes the Department's computer system to damage and loss of valuable data.

The Department should update its written policies and procedures regarding the disaster recovery plan. Further, the plan should be tested on a regular basis and stored in a secured off-site location. The disaster recovery plan should include the following:

*Specific information for the
disaster recovery plan*

- ✓ Personnel assigned to disaster recovery teams and their emergency telephone numbers.
- ✓ A risk analysis identifying critical applications, exposures, and an assessment of potential impact on the Department.
- ✓ Arrangements with vendors to support hardware and software requirements.
- ✓ A designated physical facility offsite.

The Department's personnel files should contain current employee data

Personnel and payroll controls help ensure that employees' wages are supported by personnel data and are the proper amounts. Specifically, the Department should ensure that current personnel action forms, insurance benefits election forms, and direct deposit authorization forms are maintained in its personnel files. Although the Department had established appropriate internal control policies and procedures, it was unable to locate the following documents for numerous employees:

- Current personnel action forms to support the employee's pay rate.
- Insurance benefit election forms.
- Direct deposit authorization forms.

A finding similar to this one was reported previously.

To help ensure payroll and payroll-related expenditures are properly supported and compliance with payroll laws and regulations, the Department should always follow its established policies and procedures.

The Department needs to comply with federal laws and regulations

The Department administers several federal programs to serve individual recipients throughout the State of Arizona. Consequently, the Department is responsible for complying with federal requirements outlined in the United States Code; Code of Federal Regulations (CFR); and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. For the year ended June 30, 2001, the Department did not always comply with the federal regulations, as evidenced by the following instances of noncompliance.

Temporary Assistance for Needy Families (TANF)

The Division of Benefits and Medical Eligibility is required to refer all single parent recipients for whom either paternity has not been established or a child support order needs to be established, modified, or enforced, to the Division of Child Support Enforcement. Referring TANF recipients to the Division of Child Support Enforcement will help increase child support collections. 45 CFR §264.30 (a)

The Division of Benefits and Medical Eligibility did not refer two single parent TANF recipients to the Division of Child Support Enforcement.

Child Support Enforcement

The Division of Child Support Enforcement is required to establish support obligations within 90 days after locating the noncustodial parent, develop a system for closing child support cases that specifies each eligibility requirement and a timeline in which the cases are to be closed, and monitor subrecipients' activities to ensure that they are in compliance with federal regulations. 45 CFR §303.4 (d), §303.11, and §92.40 (a)

Auditors noted the following instances of noncompliance with the described federal requirements.

- In one case, the Division located the non-custodial parent but had not established the support obligation 6 months later.
- The Division did not close five child support enforcement cases within the time frames outlined in its policies and procedures.
- The Division took corrective action on two subrecipients' single audit findings only after auditors brought the matter to its attention.

*Rehabilitation Services – Vocational Rehabilitation Grants to States
(Vocational Rehabilitation)*

The Division of Employment and Rehabilitation Services is responsible for administering the Vocational Rehabilitation program, assisting individuals with preparing for, securing, retaining, or regaining an employment outcome that is consistent with the individual's overall ability. The Division is required to determine an applicant's eligibility for vocational rehabilitation services within 60 days, complete an assessment and individualized plan of employment for each eligible recipient, and amend the individualized plan for substantive changes. Further, if a recipient is determined to be ineligible after previously receiving services, the Department must provide a full consultation, inform the person in writing of the ineligibility determination, provide information of available services, and review the determination of ineligibility within 12 months. 29 U.S. Code §722 (a) and (b), and 34 CFR §361.43

The Division did not follow the described federal requirements in the following instances.

- Determine eligibility within 60 days for 5 individuals.
- Develop an individualized plan for employment for one eligible individual.
- Amend 2 recipients' individualized plan for employment to include substantive changes in services.
- Provide a full consultation, written notification of his or her ineligibility determination, or information of other available services after one individual was determined to be ineligible.

*Recommendation for
compliance with federal
requirements*

The Department should enforce its policies and procedures to ensure that its divisions are following all applicable federal requirements. Doing so will help ensure the proper administration of the Temporary Assistance for Needy Families, Child Support Enforcement, and Rehabilitation Services – Vocational Rehabilitation Grants to States programs.



ARIZONA DEPARTMENT OF ECONOMIC SECURITY

1717 W. Jefferson - P.O. Box 6123 - Phoenix, AZ 85005

Jane Dee Hull
Governor

John L. Clayton
Director

MAY 29 2002

Debra K. Davenport Auditor
General Office of the Auditor
General 2910 North 44th Street,
Suite 410 Phoenix, Arizona
85018

Dear Ms. Davenport:

Thank you for the opportunity to respond to the management letter for the financial statement audit of the Department and the single audit of the State of Arizona for the fiscal year 2000-01.

It is understood that this response will be included in the published management letter.

The Department wishes to express its appreciation to you and your staff for the time and effort invested in these audits.

Sincerely,

John L. Clayton

Enclosure

DEPARTMENT OF ECONOMIC SECURITY
RESPONSE TO THE FISCAL YEAR 2000-01
MANAGEMENT LETTER

The Arizona Industries for the Blind should improve internal controls over its accounting records and assets.

Measures implemented to strengthen controls over the Arizona Industries for the Blind's (AIB) accounting records and assets and address deficiencies noted in the audit finding include the following:

- Written procedures that require a member of management (the General Manager or his designee) not responsible for preparing, approving, or modifying the records of financial transactions to review and approve such transactions.
- The provision of training to employees in all departments on existing accounting policies and procedures to help ensure all assets and transactions are properly accounted for.
- Implementation of procedures that include the review of accounting information recorded on the system and calculations, including depreciation expense, by an employee not responsible for the original entry or calculations.

On July 1, 2001, AIB implemented an improved automated accounting system. This system, which is a fully integrated financial reporting package, is expected to provide improved accounting and reporting functionality.

The Division of Developmental Disabilities should properly reconcile its fiduciary accounts.

The Department's policies require the reconciliation of all bank accounts monthly. A review of the Division of Developmental Disabilities (DDD) fiduciary accounts indicates that for several of the accounts identified in the audit, the financial activity recorded on the system has been corrected and the accounts have been reconciled; however, there are accounts that still require further corrective action.

To correct the deficiencies, DDD will assign oversight and statewide supervisory responsibilities to a person qualified to review the accounts, train staff, ensure that fiduciary accounts are reconciled monthly, and ensure that accurate and complete financial information is maintained for each of its disabled clients.

The Department needs to improve its controls over fixed assets to ensure that they are safeguarded and its listing is accurate.

The Department has stewardship responsibility for approximately 4,000 capital assets. It is the Department's policy to follow internal control policies and procedures outlined in the *State of Arizona Accounting Manual* and comply with the requirements on a consistent basis.

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MANAGEMENT LETTER

The following is the status of the corrective action taken by the Department for the deficiencies cited in the finding as of June 1, 2002:

- The fixed assets included on the Department's listing that could not be located have been accounted for.
- The Department is in the process of re-tagging equipment items with missing property control tags.
- Correcting the tags of all identified assets with an incorrect property control tag number, model number, serial number or location is currently in process.
- Historical cost information has been recorded on the fixed assets listing for all of the assets that were listed at an estimated value, except for one, which will be corrected upon receipt of the cost information from the Department's Division of Technology Services.
- The Department will improve its consistency in completing all appropriate information on disposal forms and ensuring that the data is accurate .

The Department continues to emphasize the use of appropriate asset management procedures by personnel responsible for control of the Department's fixed assets and has implemented appropriate communication policies and internal controls to properly record the acquisition of equipment and help ensure that all equipment is properly tagged and accounted for. In addition, the Department has incorporated improved automation support to provide more complete and accurate fixed assets control system information.

The Department should protect its information system from damage and equipment failure.

The Department has hired a full-time Disaster Recovery Coordinator to develop, implement and maintain a meaningful Disaster Recovery Plan (DRP). Over the course of the past seven months, considerable progress has been made in developing a DRP. Disaster recovery teams have been formed with named personnel representing the Director's Office, Division of Technology Services, Division of Business and Finance, and Division of Employee Services and Support. Emergency phone numbers have been obtained for all team members and are contained within the DRP.

A risk analysis of the Department's data center was performed during the first phase of the DRP process to identify critical applications and exposures that will be addressed in the DRP. The DRP process includes the development of a comprehensive inventory of all hardware and software products required for the recovery of the data center. All vendors providing critical products and services were mailed a DRP RFI (Request for Information) containing seven questions. The responses establish a formal point of contact and solidify roles and

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MANAGEMENT LETTER

responsibilities following a disaster. The next step involves drafting terms, conditions and service-level agreements, where applicable.

Due to funding issues, the Department is partnering with the Arizona Department of Administration and the Arizona Department of Public Safety to investigate the feasibility of sharing a recovery site. In lieu of a standing recovery site, the Department will seek a suitable facility to support recovery activities on an emergency basis. The Department's Office of Facilities Management has documented the steps that will be taken to locate and secure a recovery site in the event of a disaster. These steps are contained within the DRP and will be tested during fiscal year 2003.

The Department's personnel files should contain current employee data.

The Department has over 10,600 employees who generate between 2,500 and 9500 documents each month to be filed by the Office of Personnel Management (OPM). To help ensure payroll and payroll-related expenditures are properly supported in compliance with payroll laws and regulations, on May 13, 2002, OPM implemented new procedures for filing documents that include productivity requirements and quality control checks. On March 18, 2002, OPM began an internal audit of every personnel file to identify and correct any existing deficiencies or inaccuracies. In addition, to identify and correct for misfiled paperwork, the OPM Processing Supervisor reviews a minimum of ten files a week.

The Department needs to comply with federal laws and regulations.

Temporary Assistance for Needy Families (TANF)

Division of Benefits and Medical Eligibility (DBME) policies and procedures include the referral of all single parent TANF recipients for whom paternity has not been established or a child support order needs to be established, modified, or enforced, to the Division of Child Support Enforcement (DCSE). Of the two singleparent TANF recipients identified in the finding that were not referred to DCSE in accordance with DBME's procedures, one was the result of a computer programming error, and the other was the result of a coding error. These errors have subsequently been corrected.

Child Support Enforcement

To help ensure that the Department is in compliance with federal regulations 45 CFR §303.4 (d), §303.11, and §92.40 (a), the Department's existing policies and procedures include the following:

DEPARTMENT OF ECONOMIC SECURITY
RESPONSE TO THE FISCAL YEAR 2000-01
MANAGEMENT LETTER

- The establishment of support obligations within 90 days after locating the noncustodial parent. To help ensure compliance with these established procedures, program monitors advise local offices of cases identified during local office reviews that are not worked within the 90-day federal timeframes.

- *A system for closing child support cases that outlines case closure time frames. To help ensure that cases are closed within the time frames outlined in the policies, effective November 27, 2001, Arizona Tracking and Locate Automated System (ATLAS) enhancements were implemented that will automatically close cases that are eligible for closure.*

- *Subrecipient monitoring policies and procedures that require follow-up and corrective action on all audit findings. To help ensure compliance with these requirements, DCSE administration forwards all subrecipient single audit report findings to the DCSE Program Evaluation Section for corrective action measures to be implemented, as appropriate.*

Rehabilitation Services - Vocational Rehabilitation Grants to States (Vocational Rehabilitation)

The Rehabilitation Services Administration's (RSA) policies and procedures include staff compliance with federal casework requirements and monitoring staff performance in complying with the requirements.

RSA is currently in the process of auditing cases Statewide and expects to complete this process at the end of June, at which time compliance with federal casework requirements, including case documentation and process requirements will be reinforced. Ongoing staff training will continue to emphasize:

- The need to make eligibility determinations within the required period of time or obtain client's consent for an extension;
- That the Individualized Plan for Employment (IPE) is a key case document for both the consumer and the agency, and that it is imperative that this document be 1) developed jointly with the client, 2) kept up to date throughout the life of the case, and 3) signed (originally and for any significant changes throughout the life of the case); and
- That the full consultation and notification of any significant decision made during the life of the case be communicated to the client not only verbally but also in writing, and, in particular, that the decision to determine an individual not eligible for service requires a separate notice of right to appeal.