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UTAH STATE AUDITOR

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MANAGEMENT LETTER NO. 04-33

March 23, 2005

Yvette Diaz, Executive Director
Department of Community and Economic Development
324 So. State Street, Suite 500
Salt Lake City, UT 84111

Dear Ms. Diaz:

We have completed our audit of the financial statements of the State of Utah for the year ended June 30, 2004. Our report thereon, dated October 29, 2004, is issued under separate cover. We have also completed the Department of Community and Economic Development's (the Department) portion of the statewide federal compliance audit for the year ended June 30, 2004. The federal programs tested as major programs at the Department were the Low-Income Home Energy Assistance Program (LIHEAP) and the Home Investment Partnership Program (HOME). Our report on the statewide federal compliance audit for the year ended June 30, 2004 should be issued by April 2005.

In planning and performing our audits, we considered the Department's internal control over the administration of major federal programs in order to determine our auditing procedures for the purpose of expressing our opinion on the State's compliance with the requirements of its major programs and not to provide assurance on internal control. We noted certain matters involving the Department's internal control over the administration of federal programs that we consider to be reportable conditions. These conditions are identified in the accompanying table of contents and are described in the accompanying schedule of findings and recommendations.

None of the reportable conditions is believed to be a material weakness to the State's financial statements. However, we noted a certain matter involving internal control over the administration of federal programs that we consider to be a material weakness to the Low-Income Home Energy Assistance Program. This matter is described in attached finding and recommendation Number 1.

Reportable conditions are defined as matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the organization's ability to record, process, summarize,

and report financial data consistent with the assertions of management in the financial statements or administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants. We have also identified as reportable conditions those instances of noncompliance that are required to be reported in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States and Federal OMB Circular A-133.

Material weaknesses are conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited or that noncompliance with applicable requirements of laws, regulations, contracts and grants that would be material in relation to a major program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

During our audit, we also noted other matters involving the internal control over financial reporting and compliance of the Department and its operations. We are submitting for your consideration related recommendations designed to help the Department make improvements and achieve operational efficiencies. These matters are described in the accompanying schedule of findings and recommendations.

This report by its nature focuses on exceptions, weaknesses, and problems. This should not be understood to mean there are not also various strengths and accomplishments. Our consideration of the internal control over administration of federal programs would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses.

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

We appreciate the courtesy and assistance extended to us by the personnel of the Department during the course of our audit, and we look forward to a continuing professional relationship. If you have any questions, please call Stan Godfrey, Audit Director, at 538-1356.

Sincerely,

Auston G. Johnson, CPA
Utah State Auditor

cc: Richard Bradford, Deputy Director
Gordon Walker, Community Development Division Director
Kimberley Schmeling, Budget and Accounting Supervisor
Sherm Roquero, LIHEAP Program Manager
Richard Walker, Housing Administrator

DEPARTMENT OF COMMUNITY AND ECONOMIC DEVELOPMENT

FOR THE FISCAL YEAR ENDED JUNE 30, 2004

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FINDINGS AND RECOMMENDATIONS FOR THE FISCAL YEAR ENDED JUNE 30, 2004

LOW-INCOME HOME ENERGY ASSISTANCE PROGRAM (LIHEAP)

1. INADEQUATE CONTROL OVER THE 269A FINANCIAL REPORT (Material Weakness)

Federal Agency: **DHHS**

CFDA Number and Title: **93.568 Low Income Home Energy Assistance**

Federal Award #: **G-0201UTLIEA, G-0201UTLIE2, G-0201UTLIE3, G-04B1UTLIEA**

Questioned Cost: **N/A**

Pass-through Entity: **various**

The Department of Community and Economic Development (the Department) does not perform an adequate review of the 269A Financial Reports. As a result, errors occurred for two out of the four 269A reports reviewed. First, grant award information was inaccurately reported and included expenditures for the contingency and leveraging incentive awards that were closed out in the previous fiscal year. This resulted in the \$967,951 overstatement of current and cumulative grant expenditure amounts as well as authorized federal funds for the one reported award. Second, grant award expenditures were overstated and unobligated award amounts were understated (net amount of \$7,030,398) due to the inadvertent switching of these report amounts. Adequate reviews of the financial reports are necessary to ensure accurate reporting of program activity and compliance with federal reporting requirements.

Recommendation:

We recommend that the Department perform adequate reviews of the 269A reports to ensure the accuracy of financial report information submitted to the Federal Government. In addition, we recommend that the Department submit amended 269A reports to correct reporting discrepancies.

Department's Response:

We concur with the recommendation. We will take greater care to ensure that all reports are prepared accurately. The first oversight occurred as a result of a change in the manner in which grants are issued to the State. Older grants, which may have included the main award, contingency funds and leveraging incentive funds, were issued with separate document numbers; new grants (even those with several appropriations) are issued under a single document number. While supporting documentation fully supported all expenditures and revenues, staff inadvertently reported contingency/leveraging funds expended and drawn from an old grant, with the main grant expenditures. Corrected reports have been submitted and separate the expenditures by document number.

In the second portion of the finding, we acknowledge that the amounts reported as expended and unobligated were simply transposed on the 269(A) report. However, the supporting

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documentation for the report was completely accurate and fully reconciles to the Payment Management System and the State Accounting System. HHS/OCS has never questioned the report we submitted to them. Corrected reports have been submitted.

*Contact Person: Kimberly Brown Schmeling, (801) 538-8727
Corrective Action Completed By: March 31, 2005*

2. IMPROPER FINET RECONCILIATION OF LIHEAP PROGRAM ACTIVITY (Reportable Condition)

Federal Agency: **DHHS**
CFDA Number and Title: **93.568 Low Income Home Energy Assistance**
Federal Award #: **G-03B1UTLIEA & G-04B1UTLIEA**
Questioned Cost: N/A
Pass-through Entity: N/A

Differences identified in month-end reconciliations were not properly investigated. As a result, two adjustments were erroneously made to resolve the differences. The program accountant incorrectly assumed that all of the program expenditures had been recorded properly in FINET (the State's accounting system), so he adjusted revenues between reporting categories to eliminate the differences identified in the reconciliations. However, the adjustments should have been made to the expenditures instead of the revenues. Although total revenues and expenditures for the grant were reported properly, revenues and expenditures between two reporting categories or award years were overstated/understated by \$426,969. Proper performance of month-end reconciliations, including investigation of reconciling differences, is necessary in order to ensure the accuracy of financial records.

Recommendation:

We recommend that the Department exercise greater care in performing month-end reconciliations by performing investigation of reconciling items prior to making corrections.

Department's Response:

We concur with this recommendation. Fortunately, the draw-down was completed in the correct grant in the HHS Payment Management System.

While we believe our processes/tools have been sufficient to track expenditures and revenues in this complicated multi-year program, we have developed one additional table to reconcile expenditures and revenues to grant year in all three of our payment/drawdown/tracking systems.

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*Contact Person: Kimberley Brown Schmeling, (801) 538-8727
Corrective Action Completed By: March 31, 2005*

3. INADEQUATE BUDGETARY CONTROL OVER EARMARKING REQUIREMENTS

The Department uses a budget tracking spreadsheet to monitor compliance with earmarking and other spending limitations. However, budget amounts are not determined in accordance with earmarking restrictions. Per federal regulations (45 CFR 96.87(i)), leveraging incentive award funds should not be included in the calculation of the 15% weatherization limitation. However, the Department established the budget amounts using total awarded funds without regard for this requirement to exclude leveraging incentive funds. Proper determination of budget amounts in accordance with earmarking restrictions is necessary in order to enable proper monitoring of program expenditures and to ensure compliance with federal requirements.

Recommendation:

We recommend that the Department exercise greater care in establishing budget amounts in accordance with federal earmarking restrictions.

Department's Response:

We acknowledge the incorrect initial commitment to the Weatherization program in the FFY02 [federal fiscal year 2002] program year exceeded the threshold. The agreement between the LIHEAP and Weatherization programs was subsequently amended and the funds were not spent on Weatherization activities.

Likewise, subsequent commitments to the Weatherization program are well within the 15% threshold. Staff will exercise great care to commit within this threshold in the future.

*Contact Persons: Sherm Roquero, (801) 538-8644, or
Kimberley Brown Schmeling, (801) 538-8727
Corrective Action Completed By: March 31, 2005*

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4. IMPROPER ACCOUNTABILITY OF PROGRAM ACTIVITY

The program accountant reported that funds are still available for weatherization contracts for the 2001 and 2002 award years (\$112,981 and \$77,030, respectively). However, the weatherization program manager had documented that all of the budgeted funds have been expended for those award years. Program managers and the program accountant should work together in order to ensure proper reporting of program activity and compliance with federal requirements.

Recommendation:

We recommend that program managers and the program accountant work together to ensure proper accountability of program activity and compliance with federal requirements.

Department's Response:

We concur with this recommendation. In fact, we implemented steps three years ago that would prevent this problem from occurring. Expenditures and draws reconcile appropriately in the most recent three years of grants. The problem originated when funding was previously provided to the Weatherization program the year following completion of the Heat season, but then transitioned to a "current year" model. The use of activity codes and reporting categories (implemented 3 years ago) has prevented this problem from occurring in recent grant years.

Contact Person: Kimberley Brown Schmeling, (801) 538-8727

Corrective Action Completed By: Already completed

HOME INVESTMENT PARTNERSHIP PROGRAM (HOME)

5. NONCOMPLIANCE WITH 24-MONTH FUNDS COMMITMENT REQUIREMENT (Reportable Condition) (Repeat Finding)

Federal Agency: **HUD**

CFDA Number and Title: **14.239 HOME Investment Partnership**

Federal Award #: **various**

Questioned Cost: **N/A**

Pass-through Entity: **N/A**

The Department has not complied with the requirement to commit HOME federal funds within 24 months of a grant award. HUD Notice CPD 01-13 states that "The commitment deadline occurs 24 months after the last day of the month in which HUD notifies the [participating

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jurisdiction]” through an award letter. The Congressional release date on the award letter is the indicator for determining the deadline and compliance is determined on a cumulative basis. The Congressional release date for the 2002 award letter was May 7, 2002; therefore, the cumulative commitments as of May 31, 2004 should have been equal to or greater than the cumulative award allocations through 2002. However, as of May 31, 2004, the Department still had \$370,402 in uncommitted funds. Monitoring and ensuring compliance with this requirement is necessary in order to prevent misuse and loss of federal funding due to noncompliance.

Recommendation:

We recommend that the Department implement controls to monitor and ensure compliance with the 24-month commitment requirement.

Department’s Response:

We concur with this recommendation. IDIS data will be updated to demonstrate compliance with HUD rules. Staff duties will be shifted so there is sufficient time and focus for staff to verify the timely posting within IDIS at commitment levels that meet HUD requirements.

Contact Person: Michael Glenn, (801) 538-8666

Corrective Action Completed By: June 30, 2005

6. ERRORS IN THE MONITORING LISTING AND INTEGRATED DISBURSEMENT AND INFORMATION SYSTEM (IDIS)

The monitoring listing used to identify applicable federal compliance requirements and track project reviews contained several errors in the reported project information. Two projects had the incorrect number of HOME assisted units and/or number of project units, which are used to identify projects that may be subject to Davis-Bacon federal requirements and to determine how often projects need to be reviewed or monitored. Another project that was canceled in 2001 was also erroneously included on the monitoring listing. One of the errors in the number of assisted units was due to a data entry error in IDIS and the other errors resulted from mistakes made while preparing the monitoring listing. Inaccurate information on the monitoring listing and in IDIS may lead to improper identification of applicable federal requirements, inadequate compliance monitoring procedures, and improper reporting and accountability of program funds.

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Recommendation:

We recommend that the Department implement controls and exercise greater care when inputting information into the monitoring listing and in IDIS in order to ensure the accuracy and completeness of reported information, proper identification of applicable federal requirements, and adequate compliance monitoring procedures.

Department's Response:

We concur with this recommendation. Prior to the audit, staff had already discovered the three errors identified and had made the appropriate corrections.

The 2001 project does not affect any compliance issues with HUD, but it has been removed from the tracking system. Staff will continue to exercise care in data entry and has developed a process for double-checking data entry, information collection and report generation.

*Contact Person: Michael Glenn, (801) 538-8666
Corrective Action Completed By: June 30, 2005*