

**DEPARTMENT OF MILITARY AFFAIRS**

**REPORT ON AUDIT  
FOR THE THREE-YEAR PERIOD ENDED  
JUNE 30, 2010**

***APA***  
**Auditor of  
Public Accounts**  
**COMMONWEALTH OF VIRGINIA**

## **AUDIT SUMMARY**

Our audit of the Department of Military Affairs for the three year period ended June 30, 2010 found the following.

- The high rate of ineligible participants and other issues in the Virginia Commonwealth Challenge Program place the federal funding of this program of \$2,560,525 for fiscal year 2010 at risk;
- Matters involving internal control and its operations requiring management's attention;
- Instances of noncompliance with applicable laws and regulations or other matters; and
- Except as noted below, proper recording and reporting of all transactions, in all material respects, in the Commonwealth Accounting and Reporting System.

During the course of our audit, we received an inquiry concerning a situation involving the potential mishandling of public funds by an employee at the Virginia Commonwealth Challenge Program (Challenge Program), housed at Camp Pendleton in Virginia Beach. As part of a State Police investigation, we reviewed transactions over a three year period and found approximately \$120,000 in questionable transactions involving a combination of state, federal, and private funds. The loss of funds was the result of a lack of internal controls, inadequate supervisory oversight, and a lack of segregation of duties. The Challenge Program employee had complete access to the petty cash account as well as some other private funds with no effective supervisory oversight. As a result, the employee had the opportunity to write checks, make deposits, and control the bank account, until Military Affairs' management reassigned these responsibilities.

Additionally, we found the Challenge Program admitted students to the program who were ineligible to participate. Federal regulations state that only students who are dropouts can participate in the program. In our sample of 40 students, we found 34 students or 85 percent were still attending school when they were accepted into the program. The number of ineligible students and the matter discussed above place all of the federal program costs of \$2,560,525 for fiscal year 2010 at risk.

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## AUDIT FINDINGS AND RECOMMENDATIONS

### Virginia Commonwealth Challenge Program

Military Affairs needs to strengthen policies and procedures over the Virginia Commonwealth Challenge Program (Challenge Program). Military Affairs runs the Challenge Program at Camp Pendleton in Virginia Beach, as part of the National Guard Youth Challenge Program. This is a national program designed for 16 to 18 year old high school dropouts, with the goal of producing graduates with values, life skills, and self-discipline in order to be productive citizens. We found the following issues related to the Challenge Program. A summary of the program expenses for fiscal year 2010 are below. We believe the significant non-compliance with various federal requirements places all of the federal program cost for fiscal year 2010, which total \$2,560,525, at risk.

#### *Improve Segregation of Duties over Challenge Accounts*

During the course of our audit, we received an inquiry concerning a situation involving the potential mishandling of public funds by an employee at the Virginia Commonwealth Challenge Program, housed at Camp Pendleton in Virginia Beach. As part of the State Police investigation, we reviewed transactions over a three year period and found approximately \$120,000 in questionable transactions involving a combination of state, federal, and private funds. The loss of funds was the result of a lack of internal controls, supervisory oversight, and a lack of segregation of duties. The Challenge Program employee had complete access to the petty cash account as well as some other private funds with no effective supervisory oversight. As a result, the employee had the opportunity to write checks, make deposits, and control the bank account, until Military Affairs' management reassigned these responsibilities.

Military Affairs' management transferred responsibility for the Challenge Program petty cash account to the Deputy Director of Fiscal Operations in the central office in Blackstone in September 2009. Military Affairs is reviewing the need for this account; however, in the meantime, the Deputy Director has primary responsibility for writing checks from the account while also performing the bank reconciliation. The Director of Fiscal Operations reviews the reconciliation as well as all checks written from the account.

Ideally, management should implement procedures for someone independent of the check preparation and deposit process to reconcile the account. It is our understanding that Military Affairs recently filled a vacant position in the Finance Office which should allow them to reassign responsibilities and better segregate petty cash functions.

#### *Improve Compliance with Eligibility Requirements in Challenge Program*

Military Affairs needs to improve compliance with federal eligibility requirements for the Challenge Program. We selected a sample of forty students that attended the program in fiscal year 2010 and reviewed their eligibility for the program based on the federal requirements. We found the following.

- Thirty four out of forty (85%) students tested did not meet the eligibility requirements set forth in the Youth Master Cooperative Agreement dated October 8, 2009, and CFR Title 32, Section 509 (e). These requirements cite individuals are eligible if they are dropouts from secondary school. Admissions staff admit students who are “at risk” of dropping out of school, but are still enrolled at a secondary school at the time their application is approved. This practice is not in compliance with the federal eligibility requirements.
- There was no documentation to support U.S. citizenship for three of forty (8%) students tested.
- There was no documentation to support the pre-screening drug tests for all twenty tested students who attended the Fall 2009 term because staff indicated that they had inadvertently lost the tests. Federal requirements state that program officials must maintain these records for three years.

We recommend Military Affairs strengthen procedures to ensure compliance with the federal requirements over the Challenge Program. Challenge Program management should consult with federal officials to ensure their eligibility practices comply with the federal requirements. Also, staff should retain documentation supporting eligibility determinations. Finally, Challenge Program management needs to adequately review and approve program expenses to ensure they are allowable under the federal requirements.

### Other Findings

Military Affairs’ Finance Office processes payroll, handles procurement, pays vendors and accounts for related financial operations of the agency. The Office has a Director of Fiscal Operations and eight other staff. During fiscal year 2010, one individual resigned to accept another position and another individual was on extended short term disability. In both instances, Military Affairs’ management did not reassign some job duties performed by these individuals. Some of the findings in the next section result from the lack of staff addressing these individuals’ duties.

### Improve Internal Controls over Small Purchase Charge Cards

Military Affairs needs to improve controls over granting access to and monitoring small purchase charge cards. There are 28 Military Affairs employees with small purchase charge cards, and fiscal year 2010 expenses charged to these cards was almost \$6 million. We found several issues related to small purchase charge cards as follows.

- There were nine individuals with credit limits of \$100,000, one individual with a \$60,000 limit and seven individuals with \$50,000 limits. We reviewed these credit limits in comparison to the individual’s job responsibilities and their expense patterns over the year for all individuals with a credit limit of \$100,000. For many of these individuals, these credit limits seem excessive. Most of the individuals did not consistently spend near their credit limits.

- One card issued in February 2009 with a credit limit of \$100,000 went unused the entire year.
- In three instances, the cardholder's purchases exceeded their credit limit for the month. In two instances, the amount exceeded was approximately \$1,000 without obtaining approval from the Department of Accounts (Accounts). In the third instance, Military Affairs was aware of the overage and obtained approval from Accounts; however, Military Affairs could not provide documentation of the approval.
- In one instance, the cardholder split a purchase to circumvent the single transaction limits (\$5,000) on the small purchase charge card.

Overall, Military Affairs needs to strengthen controls over its small purchase charge card program. Management should review who has charge cards so that only individuals who need them for their job have cards. In addition, management should review credit limits to determine if they are appropriate. Lastly, cardholders need to monitor their charge card activity to ensure they do not exceed their credit limits or split purchases to circumvent controls.

#### *Improve Internal Controls over Payroll Procedures and Recordkeeping*

Military Affairs could not provide adequate documentation to support certain payroll transactions and did not comply with state requirements for wage employees working over 1,500 hours. We analyzed payroll information for fiscal years 2008 and 2009 and found the following.

- Military Affairs could not provide adequate documentation to support various payroll transactions for Workforce Transition Act payments. We reviewed payroll transactions that exceeded a certain threshold to determine if they were reasonable and properly documented. We found three special pay transactions, two pay rate changes, and four overtime payments that all relate to Workforce Transition payments; however, Military Affairs could provide no documentation to support the transactions or their calculations.
- Eleven wage employees in fiscal year 2008 and seven wage employees in fiscal year 2009 worked in excess of 1,500 hours in the year. Department of Human Resource Management policies require approval from the agency head for any employees who work more than 1,500 hours in a year. Military Affairs did not obtain proper approval for any of the eleven employees in fiscal year 2008 and four of the employees in fiscal year 2009.

Military Affairs should maintain documentation to support all payroll transactions. Military Affairs began using the Payroll Service Bureau in August 2008, and subsequently implemented new procedures to improve payroll documentation.

In addition, Military Affairs should comply with requirements over wage employees working more than 1,500 hours in a year. To better monitor these employees, Military Affairs began using a new statewide report in fiscal year 2010. They should review this report regularly to better monitor their wage employees and ensure compliance with state requirements.

### Improve Internal Controls over the I-9 Process

Military Affairs personnel are not properly completing Employment Eligibility Verification Forms (I-9) in accordance with guidance issued by the U.S. Citizenship and Immigration Services of the U.S. Department of Homeland Security. The guidance requires that the employer document the forms of identification shown by the employee that substantiates the employees' eligibility to legally work in the United States. The employer must document the Document Title, Issuing Authority, the Document Number, and the Expiration Date of the documentation, if any. Additionally, the employer or designated representative must complete, sign, and date the form within three business days of employment.

We reviewed a sample of five I-9 forms completed in fiscal year 2009 and found the following errors, which occurred on one or more of the forms:

- Two employees did not sign and/or date the form on or before the first day of work.
- Two employees' identification did not match the appropriate list on the form.
- One employee's certification of first date of employment on the I-9 did not match the employee's hire date.
- One form did not have the certifying agency's name.

We also reviewed five I-9 forms completed in fiscal year 2010 and found similar errors in one of these forms.

We recommend that Military Affairs' management develop steps to continuously review the I-9 process, train Military Affairs' staff on the requirements of completing I-9 forms, and develop procedures to continuously review all or a sample of I-9 forms for compliance with federal regulations. Weaknesses in the I-9 process could result in fines and penalties against Military Affairs.

### Strengthen Recording and Tagging of Equipment

Military Affairs is not recording acquisition or dispositions of fixed assets in the fixed asset system (FAACS) or tagging equipment on a timely basis. In early January 2010, the individual responsible for these functions took a position with another agency. Since that time, the position is vacant and management has not reassigned these responsibilities to other staff.

As a result, the Finance Office did not tag or record fixed assets in FAACS for the last six months of fiscal year 2010. In addition, the Office has not performed timely reconciliations of FAACS to the accounting system for this same period. It is our understanding that Military Affairs is working with the Department of Accounts to correct this situation.

The primary function of these controls is to safeguard and ensure accurate recording of fixed asset values. The Commonwealth Accounting Policies and Procedures Manual as well as federal requirements require that agencies enter their fixed assets into FAACS as soon as practicable, and tag equipment at the time of physical receipt or as soon thereafter as possible. We recommend that management immediately reassign the responsibility for tagging and recording fixed assets.

AGENCY HIGHLIGHTS

The Department of Military Affairs (Military Affairs) administers the Army and Air National Guards of Virginia as well as the Virginia Defense Force. While the Army and Air National Guards are simultaneously state military forces as well as reserve components of the Armed Forces of the United States, the Virginia Defense Force is solely a state reserve militia, composed of community volunteers, trained to augment civil agencies and military forces with trained specialists and specialized teams during emergencies.

Military Affairs has a dual state and federal mission. Military Affairs' number one state priority is preparedness to answer the Governor's call in times of emergency. The agency's number one federal priority is to answer the President's call in times of war or during national emergency. To achieve the state requirement, as well as to meet the increasing demands of their federal mission, the Department of Military Affairs must maintain a fully manned and highly trained, responsive, and motivated force.

Military Affairs receives funding through multiple sources, but the agency's primary funding source is federal funds. Military Affairs uses the majority of its funding for activities related to maintaining the National Guard. This involves providing training, maintaining armories and equipment, and also paying Guard members when activated. Military Affairs also provides tuition assistance for members of the National Guard and runs an at-risk youth program. The following tables show budget and actual activity for Military Affairs by program over the last three years.

**Analysis of Budget and Actual Expenditures by Program**

**Fiscal Year 2008**

<u>Program</u>	<u>Original Budget</u>	<u>Final Budget</u>	<u>Expenses</u>
Higher Education Student Financial Assistance	\$ 3,043,921	\$ 2,866,684	\$ 2,601,865
At-Risk Youth Residential Program	3,720,732	3,776,167	3,662,910
Defense Preparedness	28,662,849	34,305,674	33,541,455
Disaster Planning and Operations	-	129,976	129,975
Administrative and Support Services	<u>5,202,490</u>	<u>5,376,876</u>	<u>5,318,184</u>
Total	<u>\$40,629,992</u>	<u>\$46,455,377</u>	<u>\$45,254,389</u>

**Fiscal Year 2009**

<u>Program</u>	<u>Original Budget</u>	<u>Final Budget</u>	<u>Expenses</u>
Higher Education Student Financial Assistance	\$ 3,047,717	\$ 3,882,232	\$ 2,457,189
At-Risk Youth Residential Program	4,197,311	4,109,979	3,915,159
Defense Preparedness	29,374,781	37,798,624	36,741,047
Disaster Planning and Operations	-	181,368	181,339
Administrative and Support Services	<u>5,340,376</u>	<u>5,556,047</u>	<u>4,851,879</u>
Total	<u>\$41,960,185</u>	<u>\$51,528,250</u>	<u>\$48,146,614</u>

**Fiscal Year 2010**

<u>Program</u>	<u>Original Budget</u>	<u>Final Budget</u>	<u>Expenses</u>
Higher Education Student Financial Assistance	\$ 3,332,717	\$ 2,151,987	\$ 2,021,858
At-Risk Youth Residential Program	4,218,244	4,066,417	3,870,183
Defense Preparedness	28,949,054	37,844,680	33,768,525
Disaster Planning and Operations	-	1,192,000	1,192,000
Administrative and Support Services	5,492,168	5,448,832	5,033,812
Executive Management (budget reductions)	<u>(1,148,072)</u>	<u>200,000</u>	<u>-</u>
Total	<u>\$40,844,111</u>	<u>\$50,903,916</u>	<u>\$45,886,378</u>

During fiscal year 2010, Military Affairs requested and received a Treasury Loan of \$2.6 million from the Department of Treasury. This loan was necessary due to the delays in obtaining federal funding when Congress did not approve the budget in time. Military Affairs repaid this loan in three installments with the final installment being in May 2010.

Military Family Relief Fund

As part of its mission to support National Guard members and their families, Military Affairs administers the Military Family Relief Fund. The 2006 General Assembly appropriated \$500,000 in General Funds to provide relief for National Guard and armed forces reserve members and their families if they meet certain qualifications. An example of a need for which this money is available is to assist spouses of deployed soldiers, who are unable to pay their household bills due to illness or the loss of employment. The maximum assistance award is \$2,500 per need and the following table shows the activity in this fund over the last three fiscal years.

**Summary of Activity in the Military Family Relief Fund**

	<u>2008</u>	<u>2009</u>	<u>2010</u>
Beginning cash balance	\$491,877	\$445,800	\$342,127
Revenues	25,151	49,560	72,041
Expenses	<u>(71,228)</u>	<u>(153,233)</u>	<u>(47,477)</u>
Ending cash balance	<u>\$445,800</u>	<u>\$342,127</u>	<u>\$366,691</u>

Challenge Youth Program

Military Affairs also runs the Virginia Commonwealth Challenge Program (Challenge Program) at Camp Pendleton in Virginia Beach. The Challenge Program is part of the National Guard Youth Challenge Program, which is a national program designed for 16 to 18 year old high school dropouts, with the goal of producing graduates with values, life skills, and self-discipline in

order to be productive citizens. Virginia was one of the original ten pilot states in 1994, and Congress permanently authorized the program in 1998. The Challenge Program operates two residential classes per year, which begin in January and July of each year. Each class has approximately 190 students.

The program's funding is 60 percent federal and 40 percent Commonwealth General Funds. The total annual budget for the Challenge Program is approximately \$4 million and the largest expense is personal services costs for approximately 65 employees.



# Commonwealth of Virginia

**Walter J. Kucharski, Auditor**

**Auditor of Public Accounts  
P.O. Box 1295  
Richmond, Virginia 23218**

November 3, 2010

The Honorable Robert F. McDonnell  
Governor of Virginia

The Honorable Charles J. Colgan  
Chairman, Joint Legislative Audit  
and Review Commission

We have audited the financial records and operations of the Department of Military Affairs for the years ended June 30, 2008, June 30, 2009, and June 30, 2010. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

## Audit Objectives

Our audit's primary objectives were to evaluate the accuracy of recorded financial transactions on the Commonwealth Accounting and Reporting System, review the adequacy of the Department's internal controls, test compliance with applicable laws and regulations, and review corrective actions of audit findings from prior year reports.

## Audit Scope and Methodology

The Department's management has responsibility for establishing and maintaining internal control and complying with applicable laws and regulations. Internal control is a process designed to provide reasonable, but not absolute, assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

We gained an understanding of the overall internal controls, automated and manual, sufficient to plan the audit. We considered significance and risk in determining the nature and extent of our audit procedures. Our review encompassed controls over the following significant cycles, classes of transactions, and account balances for all three years in the audit period unless otherwise indicated.

Cooperative Funding Agreements (federal grant revenues)  
Petty Cash (2008, 2009 and through October 2009)  
Payroll processing  
Expenses and small purchase charge card  
Federal compliance (fiscal year 2010)

We performed audit tests to determine whether the Department's controls were adequate, had been placed in operation, and were being followed. Our audit also included tests of compliance with provisions of applicable laws and regulations. Our audit procedures included inquiries of appropriate personnel, inspection of documents, records, and contracts, and observation of the Department's operations. We tested transactions and performed analytical procedures, including budgetary and trend analyses.

### Conclusions

We found that the Department of Military Affairs properly stated, in all material respects, the amounts recorded and reported in the Commonwealth Accounting and Reporting System except for certain petty cash transactions discussed in this report. The Department records its financial transactions on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The financial information presented in this report came directly from the Commonwealth Accounting and Reporting System.

We noted certain matters involving internal control and its operation and compliance with applicable laws and regulations that require management's attention and corrective action. These matters are described in the section entitled "Audit Findings and Recommendations".

The Department has not taken adequate corrective action with respect to one audit finding reported in the prior year audit which is repeated in this letter.

### Exit Conference and Report Distribution

We discussed this report with management on November 23, 2010. Management's response to the findings identified in our audit is included in the section entitled "Agency Response." We did not audit management's response and accordingly, we express no opinion on it.

This report is intended for the information and use of the Governor and General Assembly, management, and the citizens of the Commonwealth of Virginia and is a public record.

AUDITOR OF PUBLIC ACCOUNTS

LCW: alh



# COMMONWEALTH of VIRGINIA

## DEPARTMENT OF MILITARY AFFAIRS

*Adjutant General's Office*

*Virginia National Guard*

*1100 Bank Street*

RICHMOND, VIRGINIA 23219

DANIEL E. LONG, JR.  
THE ADJUTANT GENERAL

November 23, 2010

Mr. Walter J. Kucharski  
Auditor of Public Accounts  
P O Box 1295  
Richmond, VA 23218

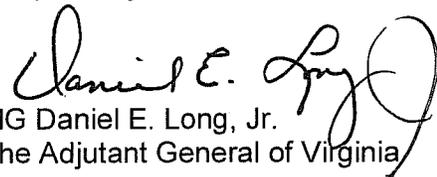
Dear Mr. Kucharski:

Attached is our response to the Auditor of Public Accounts' audit report for state fiscal years 2008, 2009, and 2010.

We appreciate your time and efforts in conducting the audit and will make every effort possible to make program changes, improve internal controls, and meet compliance requirements in the future. As you will see in our response, some changes have already been implemented.

If you have questions regarding this report, please contact Linda Coleman, Director of Fiscal Operations, at (434) 298-6419.

Respectfully,



MG Daniel E. Long, Jr.  
The Adjutant General of Virginia

cc: Brig Gen Wayne Wright  
COL Daryl Francis  
Mrs. Linda Coleman  
Mr. Steve Huxtable  
File

Department of Military Affairs  
Response to the Auditor of Public Accounts' Audit Report  
For Fiscal Years 2008, 2009, and 2010

*Improve Segregation of Duties over Challenge Accounts*

**Concur:** DMA has closed the account containing private funds. Two vacant positions in the Finance Office were filled recently and reconciliation of the Petty Cash account can now be handed over to the Reconciliations Senior Accountant as soon as training of the new individual is complete.

**Responsible Position:** Director of Fiscal Operations

**Due Date:** December 31, 2010

*Improve Compliance with Eligibility Requirements in Challenge Program*

**Concur:** Due to a misinterpretation of Challenge eligibility requirements, Challenge management allowed ineligible students to apply and be accepted into the program. This will be corrected when students are accepted into future classes. The appropriate Challenge staff will be trained regarding proper documentation requirements and file maintenance periods.

**Responsible Position:** Challenge Director

**Due Date:** January 31, 2011

*Improve Internal Controls over Small Purchase Charge Cards*

**Concur:** DMA management has performed an analysis of monthly credit limits, and as a result of this analysis, we cancelled 1 cardholder's account and made changes to monthly credit limits for 8 cardholders based upon past usage patterns and unit procurement needs. We moved the Program Administrator (PA) responsibilities to a position that should have more time to monitor card holder usage and perform other PA responsibilities, and we made the new PA aware of the importance of obtaining and maintaining written approval from the Department of Accounts (DOA) for any requests to increase monthly spending limits. Also, cardholders have been made aware that Bank of America does not deny charges that exceed the cardholder's monthly limit so they must closely monitor their own monthly spending.

**Responsible Position:** Director of Fiscal Operations

**Due Date:** Complete

*Improve Internal Controls over Payroll Procedures and Recordkeeping*

**Concur:** In August 2008, DMA moved its payroll function to DOA's Payroll Service Bureau (PSB). We believe this action has improved the types of documentation used to support payroll transactions. In May 2009, DOA began issuing a monthly report from the payroll system (CIPPS) that DMA now uses to more closely monitor the hours worked by wage employees so proper approval may be obtained in advance of any employees exceeding their work hour limits.

**Responsible Position:** Director of Fiscal Operations

**Due Date:** Complete

Improve Internal Controls over the I-9 Process

**Concur:** DMA has provided additional training to agency staff responsible for completion of I-9 forms. Also, we will implement a review process to ensure proper completion of all I-9 forms.

**Responsible Position:** Director of Personnel and Administration

**Due Date:** December 31, 2010

Strengthen Recording and Tagging of Equipment

**Concur:** The position responsible for performing all fixed asset functions became vacant in January 2010. These tasks were reassigned, but were not performed for the remainder of the fiscal year because of the heavy workload. There was no other employee to whom these tasks could be reassigned due to other office vacancies and heavy workloads maintained by all staff members. The position is now filled, the employee is being trained, and the workload will become current by the end of FY 2011.

**Responsible Position:** Director of Fiscal Operations

**Due Date:** June 30, 2011

DEPARTMENT OF MILITARY AFFAIRS

Major General Robert B. Newman, Jr.  
Adjutant General until June 10, 2010

Brigadier General Wayne Wright  
Acting Adjutant General as of June 10, 2010

Colonel Donald Sutherland  
United States Property and Fiscal Officer

Colonel Daryl Francis  
Director of Joint Staff

Linda L. Coleman  
Director of Fiscal Operations

Stephen Huxtable  
Director of Personnel and Administration