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United States General Accounting Office  
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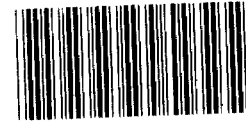
Human Resources  
Division

RELEASED

B-197985

March 10, 1980

The Honorable Jim Sasser — *James R.*  
The Honorable Howard H. Baker, Jr.  
United States Senate



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The Honorable Frank Horton  
The Honorable James H. Quillen  
House of Representatives

Subject: *[*Alleged Financial Irregularities at the Upper East Tennessee Human Development Agency, Kingsport, Tennessee*]* (HRD-80-68)

You requested that we review the use of Federal funds by the Upper East Tennessee Human Development Agency (UETHDA) located in Kingsport, Tennessee. *DLG-04086*

UETHDA is a public agency that develops and operates community action and other human resource programs in eight Tennessee counties (Washington, Sullivan, Carter, Greene, Hawkins, Johnson, Unicoi, and Hancock). UETHDA receives funding from the Community Services Administration (CSA), other Federal agencies, and State and local agencies. Funding for 1979 from these sources totaled about \$3 million.

*AGC00177*  
*DLG-04087*  
*DLG-04088*

When we received your requests, the Division of State Audits, Tennessee Comptroller of the Treasury, was making a comprehensive review of UETHDA's financial operations and records. Accordingly, as discussed with your offices, we limited our work to monitoring the State's audit. We also reviewed the results of an investigation by CSA's Inspection Division and audits for fiscal years 1975-77 by the certified public accounting (CPA) firm retained by UETHDA.

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The State audit and the CSA investigation disclosed questionable financial practices. These practices involved making retroactive lump-sum payments to certain UETHDA officials from a pension fund established without CSA approval, advancing vacation pay and salaries to certain employees, and making interest-free loans to employees. The State audit also identified numerous deficiencies in UETHDA program management.

We met with your staffs and discussed the findings from the CSA investigation and the State audit. We also discussed actions taken or planned by UETHDA and CSA. As your staffs requested, we have summarized the information we obtained in this letter. Arrangements have been made to have a copy of the State audit report sent to you when it is issued.

INVESTIGATION OF UETHDA ACTIVITIES  
BY CSA'S INSPECTION DIVISION

CSA's Inspection Division received inquiries about the propriety of a pension plan instituted by the executive director of UETHDA, which provided for retroactive lump-sum payments to himself and certain UETHDA officials. The Inspection Division's November 1978 report on its investigation of these inquiries discussed the pension plan in considerable detail, as well as several other matters.

The CSA investigation disclosed that the UETHDA executive director presented a pension plan to his board of directors in March 1978. The plan, which was only briefly outlined, was quickly approved by the board on March 16. Three days before the plan was presented to the board, a \$1,200 check was drawn for the executive director as partial payment under the plan. While the proposed plan was to benefit all eligible UETHDA employees, it provided for retroactive lump-sum payments to only certain top UETHDA officials. Lump-sum payments, essentially funded from CSA grants, were made to the executive director and three other officials:

Executive director	\$10,200
Program director	3,400
Equal opportunity officer	2,800
Fiscal officer	4,200

The proposed plan was submitted by the chairman of the UETHDA board of directors to the CSA regional office. On November 13, 1978, the regional office instructed UETHDA to make no further payments under the plan. The regional office also questioned whether the lump-sum payments constituted bona fide pension payments. In its response to the board, the regional office stated:

"\* \* \* The payments were not deposited to the plan as credits to the employees but rather given to them in the form of bonuses. This is further evidenced since the employees receiving the checks had not contributed to the plan."

The CSA investigation report also discussed certain other questionable financial transactions dealing with

- advancing vacation pay and salaries to certain employees,
- making interest-free loans to some employees, and
- using funds provided for approved projects to underwrite an economic development business venture that neither UETHDA's board of directors nor CSA approved. (The State auditors questioned about \$18,000 in UETHDA expenditures on this project.)

CSA forwarded a copy of its UETHDA report to the U.S. Attorney for the Eastern District of Tennessee for possible criminal prosecution, but according to a CSA official, the Department of Justice declined to pursue the matter.

#### INVESTIGATION BY STATE AUDITORS

A local official requested the State audit agency to investigate UETHDA because of publicity about its activities.

In January 1979, following the CSA investigation, the Division of Audit, Tennessee Comptroller of the Treasury, began to review UETHDA's financial activities. The audit was completed in September 1979, and a draft report was forwarded to UETHDA for comment.

In addition to employee loans and advances and payments made under the pension plan--findings similar to those

reported by the CSA investigation--the State auditors cited UETHDA for other program deficiencies. The auditors identified 22 deficiencies in UETHDA program management and questioned about \$222,000 in costs charged to various programs during fiscal years 1976-78.

The State auditors had the following observations about UETHDA's program management and accounting system:

--Ineffective program management--the executive director failed to adequately supervise his immediate subordinates; there was a lack of communication at all levels; the fiscal officer was responsible directly to the executive director instead of the finance committee or the executive committee; and program directors failed to take appropriate actions to correct deficiencies that could delay or lose funding.

--Inadequate accounting system--there was no segregation of duties among the bookkeepers; UETHDA had about 35 different bank accounts, with each program using one or more accounts; UETHDA did not have adequate methods of recording cash receipts or disbursements; a general journal to explain adjusting journal entries was not kept; and UETHDA had not established a fiscal year for operations.

In responding to the State's draft report, UETHDA totally concurred with 19 findings and basically concurred with the other 3, but it did not agree in all cases with the State's questioned costs. UETHDA officials believe they can support some of the costs questioned before the State's final report is issued. The final report was not available to us at the writing of this report.

#### AUDITS BY UETHDA'S CPA FIRM

UETHDA has been using the same CPA firm since 1965. The firm's 1975-77 audit reports stated that:

"The accounting system and internal controls of Upper East Tennessee Human Development Agency are considered adequate to safeguard its assets, check the accuracy and reliability of the accounting data, promote operating efficiency and

encourage compliance with prescribed management policies and any additional fiscal responsibilities and accounting requirements established by CSA."

After a quality assurance review of the CPA firm's 1977 report on UETHDA activities, the CSA regional auditor said that he believed the firm had performed the audit adequately and in accordance with generally accepted auditing standards. He pointed out, however, that the firm had failed to include in its report many questionable items included in the working papers. As a result of the auditor's evaluation, the CPA firm amended its 1977 report to include additional questionable costs, such as salary advances, advanced vacation payments, and salaries paid at rates in excess of amounts authorized by CSA.

However, the State auditors were not satisfied with the CPA firm's performance and reported the firm to the State board of accountancy. As of February 1980 we had not been advised of the board's decision.

CSA REGIONAL ASSISTANCE  
TO UETHDA UNTIMELY

Although the CSA regional office gave UETHDA guidance and assistance, the UETHDA director cited several instances where he believed that responses to requests for assistance were untimely:

- In April 1979, UETHDA asked for approval to retain an attorney to provide legal guidance to its board during the UETHDA controversy. Approval was granted 3 months later.
- In July 1979, UETHDA requested the CSA regional office to verify in writing that its board chairman had not visited the regional office in Atlanta as the chairman had claimed on a travel voucher--the request was not answered until December 1979.
- Also in July 1979, UETHDA requested permission to spend about \$265 for an actuarial study to determine the cost of participating in the Tennessee Consolidated Retirement System--as of February 1980, the regional office had not responded to this request.

UETHDA ACTIONS

The following are some changes that have taken place at UETHDA in the past several months:

- The executive director involved in some of the questionable financial activities has resigned.
- The new executive director seems to be committed to getting UETHDA back on its feet and enhancing its public image.
- UETHDA's board of directors has some new members and a new chairman.
- A new accounting system is in operation.
- UETHDA has found that it may be eligible to participate in a State retirement plan, and it is actively pursuing coverage under that plan.
- UETHDA's bylaws have been rewritten to provide for a finance committee to monitor financial operations and to serve as a liaison between the fiscal department and the full board.

At UETHDA's request, the Tennessee Comptroller of the Treasury has agreed to be UETHDA's independent auditor; the State's audit of UETHDA's 1979 transactions was scheduled to begin in early February 1980.

According to UETHDA's new executive director, the fiscal officer has repaid the \$4,200 paid under the pension plan, and an installment plan has been negotiated with the equal opportunity officer for repaying the \$2,800 lump-sum pension payment made. UETHDA is also planning to bring legal action against those still owing money because of their participation in the pension plan and because of advanced salary and vacation pay; action will be initiated when the State's final report is issued.

CSA ACTION

The CSA regional office has increased its visits to UETHDA, and it has helped UETHDA establish its new accounting system. However, for the most part, the CSA regional

office has been awaiting the outcome of the State audit of UETHDA activities. In March 1979 the CSA regional director told the chairperson of the UETHDA board of directors that CSA would "withhold action relating to your agency's financial management practices until the audit is completed and we receive an official copy of the audit report."

Officials at the CSA headquarters office stated that CSA would help UETHDA strengthen and improve its operations. They said that CSA would

- make more onsite visits,
- provide more technical assistance, and
- provide more intensified training to board members.

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In view of the State's comprehensive examinations of UETHDA's financial activities, UETHDA's general agreement with the findings of the State's audit and its implementation of recommendations in the State's draft report, and CSA's willingness to help UETHDA improve its management and fiscal controls, we believe that additional work by us at this time is not warranted.

As arranged with your offices, unless you publicly announce its contents earlier, we plan no further distribution of this report for 10 days. At that time, we will send copies to interested parties and make copies available to others upon request.

  
Gregory J. Ahart  
Director