



**OFFICE OF AUDITOR OF STATE
STATE OF IOWA**

David A. Vaudt, CPA
Auditor of State

State Capitol Building
Des Moines, Iowa 50319-0004

Telephone (515) 281-5834 Facsimile (515) 242-6134

NEWS RELEASE

FOR RELEASE _____

August 29, 2008

Contact: Andy Nielsen
515/281-5834

Auditor of State David A. Vaudt today released a report on the Iowa Department of Economic Development for the year ended June 30, 2007.

The Department's purpose is to enhance the economic development of Iowa and provide for job creation and increased prosperity and opportunities for citizens.

A copy of the report is available for review in the Iowa Department of Economic Development, in the Office of Auditor of State and on the Auditor of State's web site at <http://auditor.iowa.gov/reports/reports.htm>.

###

**REPORT OF RECOMMENDATIONS TO THE
IOWA DEPARTMENT OF ECONOMIC DEVELOPMENT**

JUNE 30, 2007

Office of
**AUDITOR
OF STATE**
State Capitol Building • Des Moines, Iowa



David A. Vaudt, CPA
Auditor of State



OFFICE OF AUDITOR OF STATE
STATE OF IOWA

David A. Vaudt, CPA
Auditor of State

State Capitol Building
Des Moines, Iowa 50319-0004

Telephone (515) 281-5834 Facsimile (515) 242-6134

August 27, 2008

To Michael L. Tramontina, Director of the
Iowa Department of Economic Development:

The Iowa Department of Economic Development is a part of the State of Iowa and, as such, has been included in our audits of the State's Comprehensive Annual Financial Report (CAFR) and the State's Single Audit Report for the year ended June 30, 2007.

In conducting our audits, we became aware of certain aspects concerning the Department's operations for which we believe corrective action is necessary. As a result, we have developed recommendations which are reported on the following pages. We believe you should be aware of these recommendations which include those reported in the State's Single Audit Report and the State's Report on Internal Control, as well as other recommendations pertaining to the Department's internal control and compliance with statutory requirements and other matters. These recommendations have been discussed with Department personnel and their responses to these recommendations are included in this report.

This report, a public record by law, is intended solely for the information and use of the officials and employees of the Iowa Department of Economic Development, citizens of the State of Iowa and other parties to whom the Iowa Department of Economic Development may report. This report is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of the Department during the course of our audits. Should you have questions concerning the above matters, we shall be pleased to discuss them with you at your convenience. Individuals who participated in our audits of the Department are listed on page 12 and they are available to discuss these matters with you.


DAVID A. VAUDT, CPA
Auditor of State


WARREN G. JENKINS, CPA
Chief Deputy Auditor of State

cc: Honorable Chester J. Culver, Governor
Charles J. Krogmeier, Director, Department of Management
Timothy C. Faller, Acting Director, Legislative Services Agency

June 30, 2007

Findings Reported in the State's Single Audit Report:

CFDA Number: 14.228 – Community Development Block Grants/State's Program
Agency Number: B-05-DC-19-0001, B-06-DC-19-0001, B-07-DC-19-0001
Federal Award Year: 2005, 2006, 2007

State of Iowa Single Audit Report Comment: 07-III-HUD-269-1

Subrecipient Monitoring – Under the Community Development Block Grant (CDBG) program, housing rehabilitation grants may only be awarded to local governments. A local government may administer the program or may enter into a subrecipient agreement with an administrative entity, such as a Council of Governments, to administer the program. When a local government enters into such an agreement, the government effectively passes down all federal requirements of the program to the administrative entity, except for approving final reports and requesting funds. The agreement may not identify the administrative entity as a subrecipient when, in fact, the administrative entity becomes a subrecipient and must comply with CDBG program and OMB Circular A-133 requirements upon entering into the agreement. In addition, upon entering into the agreement, the local government is responsible for monitoring the administrative entity for compliance with CDBG and OMB Circular A-133 requirements.

The Department has not advised local governments that administrative entities become subrecipients upon execution of an agreement in which the administrative entity agrees to administer the program. In addition, the Department has not made local governments aware of subrecipient monitoring requirements under OMB Circular A-133.

Recommendation – The Department should develop and implement policies and procedures to ensure local governments are aware of the subrecipient relationship created when the local government enters into a subrecipient agreement with an administrative entity to administer the program. The policies and procedures should include the subrecipient monitoring procedures required under OMB Circular A-133.

Response and Corrective Action Planned – The Department attempted to address some of the issues relating to subrecipient agreements in the 2007 program year, including a nine-point explanation of subrecipient parameters and requirements. In response to the finding noted above, the Department now plans to add additional language to the Management Guide to explain to local governments when any of the functions of a project such as, general administration, technical services, or the “full-service” activities that require a detailed subrecipient agreement, are contracted out to an administrative entity the federal and state regulations related to those contracted activities pass through to the Council of Governments or other administrative entity.

The Management Guide will also clarify to the local government their responsibility for monitoring the administrative entity and ensuring the entity complies with all applicable federal and state regulations. If an administrative entity performs many of the program functions on behalf of the local government, particularly the receipt and payment of bills without prior local government approval, then a more detailed subrecipient agreement will be required, rather than a simple administrative agreement and/or technical services contract. The subrecipient agreement and the relationship between the local government and the administrative entity will be required to be consistent with the Department's “Subrecipient Agreement Usage Parameters” as noted in the Management Guide.

Report of Recommendations to the Iowa Department of Economic Development

June 30, 2007

In addition to the aforementioned items being added to the Management Guide, the Department will provide the information at the annual Recipient Workshop attended by local governments and their administrative entities.

Conclusion – Response accepted.

CFDA Number: 14.228 – Community Development Block Grants/State’s Program
Agency Number: B-05-DC-19-0001, B-06-DC-19-0001, B-07-DC-19-0001
Federal Award Year: 2005, 2006, 2007

CFDA Number: 14.239 – HOME Investment Partnerships Program
Agency Number: M-05-SG-19-0001, M-06-SG-19-0001, M-07-SG-19-0001
Federal Award Year: 2005, 2006, 2007

State of Iowa Single Audit Report Comment: 07-III-HUD-269-2

Cash Management – Effective cash management procedures provide for minimizing the amount of time between the drawdown/request for federal funds and the disbursement of those funds. As stated in the Cash Management Improvement Act (CMIA) Agreement, the CDBG and HOME programs are funded on a pre-issuance basis. This means federal draws are not to be deposited more than three days prior to the date of disbursement.

A review of the Department’s ledgers and cash management system identified one of fifteen payroll draws for CDBG and one of twenty-four payroll draws for HOME were not drawn within the proper time period.

Recommendation – The Department should develop and implement procedures to ensure federal funds are drawn in amounts sufficient to cover current needs and are disbursed in a timely manner without carrying excessive daily balances.

Response and Corrective Action Planned – The draw noted above for both CDBG and HOME was not drawn within the proper time period due to an employee vacation. The Department will implement procedures to ensure draws are made within the proper time period in all instances, including employee vacations.

Conclusion – Response accepted.

CFDA Number: 14.228 – Community Development Block Grants/State’s Program
Agency Number: B-05-DC-19-0001, B-06-DC-19-0001, B-07-DC-19-0001
Federal Award Year: 2005, 2006, 2007

CFDA Number: 14.239 – HOME Investment Partnerships Program
Agency Number: M-05-SG-19-0001, M-06-SG-19-0001, M-07-SG-19-0001
Federal Award Year: 2005, 2006, 2007

State of Iowa Single Audit Report Comment: 07-III-HUD-269-3

Performance and Evaluation Report (OMB No. 2506-0085) – An annual Performance and Evaluation Report is due from each federal grantee within ninety days of the close of its program year in a format suggested by the U.S. Department of Housing and Urban Development (HUD). HUD encourages submissions of the report in both paper and

Report of Recommendations to the Iowa Department of Economic Development

June 30, 2007

computerized formats. Among other factors, the report is to include a description of the use of funds during the program year and an assessment of the grantee's use for the priorities and objectives identified in its plan.

The Department's 2006 Annual Performance and Evaluation Report overstated the units produced by 100 units in the "Investment of Available Resources" section and "Households Assisted with Housing for Other Renters" was understated by 154 households.

Recommendation – The Department should review the Annual Performance and Evaluation Report prior to submission to ensure accurate reporting of the Department's performance measures.

Response and Corrective Action Plan – The overstatement of units in the "Investment of Available Resources" section and understatement of units in the "Households Assisted with Housing for Other Renters" section was due to an error when transferring the figures from staff work papers to the report. The Department will make every effort in the future to ensure the figures are transferred accurately.

Conclusion – Response accepted.

CFDA Number: 14.228 – Community Development Block Grants/State's Program

Agency Number: B-05-DC-19-0001, B-06-DC-19-0001, B-07-DC-19-0001

Federal Award Year: 2005, 2006, 2007

State of Iowa Single Audit Report Comment: 07-III-HUD-269-4

Subrecipient Monitoring – OMB Circular A-133 requires a pass-through entity to be responsible for monitoring the activities of the subrecipients, as necessary, to ensure federal awards are used for authorized purposes and in compliance with laws, regulations and provisions of the contract or grant. The Circular also requires each state to ensure required audit reports of subrecipients are completed within nine months of the end of the subrecipient's audit period, issue a management decision on audit findings within six months of receipt of the subrecipient's audit report and ensure the subrecipient takes timely and appropriate corrective action on all audit findings.

- (a) The Department has established policies and procedures to be followed in the performance of subrecipient monitoring. In accordance with policies, the Department must ensure funds are not expended or obligated before the Department approves the subrecipient's request for release of funds (RROF). For two of twenty-five CDBG project files tested, the RROF letter was appropriately included in the file. However, the RROF publication notice was not located in the project file.
- (b) The Department has established policies and procedures to review audit reports for subrecipients who expend more than \$500,000 in federal awards from the Department each year. For three of eight CDBG project files tested, an informal review was conducted. However, a formal review was not completed. The findings were noted on the cover of the annual report, but not reported on the review sheet in accordance with policies. Additionally, no follow-up was conducted on the findings indicated.

Report of Recommendations to the Iowa Department of Economic Development

June 30, 2007

Recommendation –

- (a) The Department should ensure policies and procedures are followed to ensure all required documents have been received and approval is given prior to expending or obligating funds.
- (b) The Department should ensure audit reports are formally reviewed for all subrecipients which receive \$500,000 or more in federal awards each year.

Response and Corrective Action Planned –

- (a) For the two projects noted above, the notice was published. However, the publication notice was not included in the project file. Upon receipt of this comment, CDBG staff has obtained the publication notices and placed them in the appropriate file.
- (b) The Department currently does not complete formal review paperwork on audit reports until the close-out process for a project is underway. For the projects cited above, the audit coordinator reviewed the audit reports and noted any findings on the report. These notes would then be referred to upon close-out. For audits reviewed prior to the end of the project, any significant findings are communicated to the Project Manager for their attention during monitoring. In the future, the audit coordinator will document communication with the Project Manager in the project file to demonstrate appropriate actions are being taken in response to any significant audit findings.

Conclusion – Response accepted.

CFDA Number: 14.239 – HOME Investment Partnerships Program
Agency Number: M-05-SG-19-0001, M-06-SG-19-0001, M-07-SG-19-0001
Federal Award Year: 2005, 2006, 2007

State of Iowa Single Audit Report Comment: 07-III-HUD-269-5

Suspension and Debarment – OMB Circular A-133 states the Department is prohibited from contracting with or making awards under covered transactions to parties who are suspended or debarred. The Department has established procedures to ensure transactions are with contractors who are not suspended or debarred. The contractor eligibility form in the project file could not be located for one of ten files tested.

Recommendation – The Department should perform adequate procedures to ensure all required documentation, including contractor eligibility forms, are in the project files.

Response and Corrective Action Planned – The Contractor on this project had previously been found to not be suspended or debarred and the local project administrator assumed the previous clearance would still be in effect for this project. The Department has implemented procedures to ensure local project administrators are aware a new contractor clearance should be conducted for each new project.

Conclusion – Response accepted.

Report of Recommendations to the Iowa Department of Economic Development

June 30, 2007

CFDA Number: 21.000 – Temporary State Fiscal Relief (Jobs and Growth Tax Reconciliation Act of 2003)

Agency Number: None

Federal Award Year: 2003

State of Iowa Single Audit Report Comment: 07-III-TREAS-269-1

Subrecipient Monitoring – OMB Circular A-133 requires a pass-through entity to provide the subrecipient the federal award information (CFDA title and number, award name and number, award year, if the award is research and development and name of Federal agency) and the applicable compliance requirements. The Circular also requires the pass-through entity to notify the subrecipient of the audit requirements under OMB Circular A-133 if federal expenditures are \$500,000 or more during the subrecipient's fiscal year.

The Department did not follow established policies and procedures to provide subrecipients with the award information required. The Department has also not notified the subrecipient of the audit requirements.

Recommendation – The Department should follow policies and procedures to ensure all subrecipients are provided the required award information and applicable compliance requirements as required by OMB Circular A-133, including the requirement to have a single audit when federal expenditures are \$500,000 or more during the subrecipient's fiscal year.

The Department should ensure audit reports are formally reviewed for all subrecipients which receive \$500,000 or more in federal aid each year.

Response and Corrective Action Planned – The Department provided the CFDA title and number, amount of award, award name, and the name of the Federal awarding agency to all subrecipients via a letter sent on January 17, 2008. The letter also included the audit requirements under OMB Circular A-133 if the subrecipient's federal expenditures exceeded \$500,000 during their fiscal year.

Additionally, the letter requested all subrecipients who determined they were subject to an audit submit an audit report to the Department. These audit reports will be reviewed by the Department.

In the future, letters will be sent to subrecipients either at the time they receive their payment from the Department or immediately following the end of the State's fiscal year.

Conclusion – Response accepted.

June 30, 2007

Finding Reported in the State's Report on Internal Control:

Timesheet approval – The Department's employee timesheets are not approved by an individual who does not have the authority to enter new employees into the payroll HRIS system. An individual at the Department has the ability to enter new employees into the HRIS payroll system, approve timesheets and approve pay rate changes.

Recommendation – The Department should develop and implement policies and procedures to segregate duties so the same individual does not enter information on the HRIS payroll system and approve timesheets and pay rate changes.

Response – Effective with the pay period ended February 7, 2008, both the Administrative Division Coordinator and Accountant 3 will approve timesheets on the HRIS payroll system. The Administrative Division Coordinator and Human Resource Associate will review the pre-final payroll register. This process will provide adequate segregation of duties for the timesheet approval process.

Conclusion – Response accepted.

Other Finding Related to Internal Control:

Loans Receivable – The Department provides loans and forgivable loans through various programs. A review of the loan receivable activity identified the following:

- (a) Each forgivable loan included on the loan repayment database (LRD) has an "End Date" which is the date the Department makes a decision as to whether the loan should be forgiven or not. For the CEBA, VAAP, PIAP, Brownfield and ARC loan programs, numerous instances were noted where the "End Date" listed on the LRD was prior to June 30, 2007. However, decisions had not been made and/or documented by the Department as to whether the loans had been forgiven or not. As a result, the loan receivable balances and the related allowance for doubtful accounts could be overstated at June 30, 2007.
- (b) The Department forgave three loans, but the outstanding balances for the loans were not reduced to zero. Total loans receivable and the related allowance for doubtful accounts were overstated at fiscal year end by \$500,000. The net effect on assets and fund balance was zero.
- (c) Principal and interest on a loan are to be applied in accordance with the amortization schedule as stated in the loan contract. Many of the payments received on the HOME loan program were not applied to principal and interest appropriately according to contract terms.
- (d) In 2003, the Department converted to the LRD system. Many loan balances on the HOME loan program were carried forward incorrectly. Variances range from a small amount to thousands of dollars between loans receivable on the LRD database and the amount reported by the Department.

Report of Recommendations to the Iowa Department of Economic Development

June 30, 2007

Recommendation –

- (a) The Department should develop and implement procedures to ensure forgivable loans are analyzed by the “End Date”, a decision is made and documented as to whether the loan is forgiven or not and update the LRD system accordingly.
- (b) The Department should develop and implement procedures to ensure loan balances and the related allowance for doubtful accounts are reduced to zero when loans are formally forgiven.
- (c) The Department should develop policies and procedures to ensure principal and interest are applied properly when repayments are received.
- (d) The Department should correct the LRD database to report correct loans receivable balances.

Response –

- (a) The Department completed close-outs on 25% of the forgivable loans with an “End Date” of June 30, 2007 or prior with several more close-outs in process. Many of the remaining forgivable loans are part of a backlog the Department has been working on closing out over the past two years. While considerable progress has been made, we will continue efforts (including utilizing accounting staff) to fully complete this process.
- (b) Due to a communication problem between Loan Servicing and the staff performing close-outs, the necessary paper work needed to close-out these loans was not received by Loan Servicing. Loan Servicing will work with the staff responsible for close-outs to ensure the proper paper work is received and forgivable loans are removed from the Loan Repayment Database (LRD) in a timely manner.
- (c/d) The Department is in the process of developing a new loan processing system to be implemented as of July 1, 2008. The new system will more accurately apply principal and interest to properly reflect amortization schedules (depending on the timeliness of the receipt of payment). As the Department converts from the old system to the new system loan balances will be reviewed and any balance corrections needed will be completed.

Conclusion – Response accepted.

June 30, 2007

Findings Related to Statutory Requirements and Other Matters:

- (1) Iowa Code Compliance – The Department was not in compliance with Chapter 15.203 of the Code of Iowa during the year ended June 30, 2007. This code section created the Agricultural Products Advisory Board within the Department, with the Board to consist of five members appointed by the Director and five members appointed by the Secretary of Agriculture. The Secretary of Agriculture has only appointed three members.

Recommendation – The Department should take the necessary steps to comply with the Code of Iowa.

Response – The Department has submitted a list of possible candidates to the Secretary of Agriculture and will follow-up to check on the progress of the appointments.

Conclusion – Response accepted.

- (2) Board Minutes – Board minutes are recorded at each of the monthly Board meetings. None of the Department's fiscal year 2007 Board minutes were signed.

Recommendation – The Board minutes should be signed to authenticate the record.

Response – Effective February 2008, the Board Chair will sign the previous month's minutes at the end of the Board meeting after a motion to approve the minutes is passed by the Board.

Conclusion – Response accepted.

Report of Recommendations to the Iowa Department of Economic Development

June 30, 2007

Staff:

Questions or requests for further assistance should be directed to:

Kay F. Dunn, CPA, Manager
James S. Cunningham, CPA, Senior Auditor II
Tracy L. Daugherty, CPA, Senior Auditor
Andrew E. Nielsen, CPA, Deputy Auditor of State

Other individuals who participated on the audits include:

Tiffany Amber Berkland, Staff Auditor
Donald J. Lewis, CPA, Staff Auditor
Brian P. Schenkelberg, CPA, Staff Auditor
Marta M. Sobieszkoda, Staff Auditor
Scott G. Anderson, Assistant Auditor
Lori M. Dinville, Assistant Auditor
Keith C. Kistenmacher, Assistant Auditor
Jessica N. Meierotto, Assistant Auditor