DEPARTMENT OF FINANCE

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November 9, 2009

Mr. Steve Hardy, Director
Department of Alcoholic Beverage Control
3927 Lennane Drive, Suite 100
Sacramento, CA 95834

Dear Mr. Hardy:

Final Report—Department of Alcoholic Beverage Control Special Review

The Department of Finance, Office of State Audits and Evaluations (Finance), has completed its review of the Department of Alcoholic Beverage Control (ABC). We reviewed the adequacy of ABC's policies and procedures over its federal grant management and budgetary processes and reconstructed the Alcohol Beverage Control Fund's fund condition statements.

The enclosed report is for your information and use. We initially issued the final report on October 21, 2009; however after the report was distributed, we noted an error in Table 2 of Observation 8. To correct the error, we are reissuing the final report.

Please note that Observation 8, Table 2 has been revised to reflect $271,665 federal grant expenditures for fiscal year 2007-08. Additionally, we made minor clarifying word changes in the Executive Summary and Results section. Further, we included an evaluation of ABC's response to acknowledge the potential inability of ABC to implement recommendations for Observations 1 and 8.

In accordance with Finance's policy of increased transparency, this report will be placed on our website. Additionally, pursuant to Executive Order S-20-09, please post this report in its entirety to the Reporting Government Transparency website at http://www.reportingtransparency.ca.gov/ within five working days of this transmittal.

We appreciate the assistance and cooperation of ABC's staff. If you have any questions regarding this report, please contact Cheryl Lyon, Manager, at (916) 322-2985.

Sincerely,

David Botelho, CPA
Chief, Office of State Audits and Evaluations

Enclosure

cc: On following page

cc: Mr. Timothy Gorsuch, Chief Deputy Director, Department of Alcoholic Beverage Control
Mr. Eduardo Jimenez, Assistant Director, Administration, Department of Alcoholic Beverage Control
Mr. Steve Ernst, Assistant Director, Northern Division, Department of Alcoholic Beverage Control
Mr. Joe Cruz, Assistant Director, Southern Division, Department of Alcoholic Beverage Control
Ms. Ging Tucker, Fiscal Officer, Department of Alcoholic Beverage Control

SPECIAL REVIEW

Department of Alcoholic Beverage Control

Prepared By:
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Department of Finance

092100043

June 2009

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EXECUTIVE SUMMARY

The Department of Finance, Office of State Audits and Evaluations (Finance), conducted a review of the Department of Alcoholic Beverage Control (ABC). We reviewed the adequacy of ABC's policies and procedures over its federal grant management and budgetary processes and reconstructed the Alcohol Beverage Control Fund's (Fund 3036) fund condition statements.

The ABC's policies and procedures over its federal grant management and budgetary processes need improvement. To strengthen its operations, we recommend that ABC:

- Ensures all key processes are documented and updated regularly.
- Cross-trains staff to ensure duties can be completed in the absence of key staff.
- Reconciles its bank accounts immediately and reviews reconciliations for accuracy and propriety.
- Implements policies and procedures to ensure that proper spending authority is obtained prior to receiving and expending federal funds.
- Periodically reconciles federal grant receipts with expenditures to ensure accuracy and propriety.

Because ABC's Fund 3036 fund condition statements did not tie to the Governor's Budget or its year-end State Controller's Office (SCO) reports, we reconstructed the statements for fiscal years 2003-04 through 2007-08 (Appendix A). Our reconstruction indentified a $2.2 million discrepancy between supporting records and the amount reported in the Governor's Budget. Additionally, during our reconstruction, we found that ABC had not recorded expenditures assessed by SCO and recorded entries to its cash and fund balance that lacked supporting documentation.

We recommend ABC post a prior-year adjustment to correctly state the 2008-09 beginning fund balance. Additionally, ABC should ensure year-end SCO reports and the fund condition statement are prepared accurately and sufficient supporting documentation is retained.

Further, federal grant expenditures totaling approximately $869,805 were improperly disbursed from Fund 3036 and subsequent federal reimbursements received were not correspondingly recorded. We recommend ABC reimburse Fund 3036 for the improper expenditures and record all federal grant expenditures and reimbursements in the Federal Trust Fund (Fund 0890).

BACKGROUND, SCOPE, AND METHODOLOGY

BACKGROUND

The Department of Alcoholic Beverage Control (ABC) is vested with the exclusive power to license and regulate persons and businesses engaged in the manufacture, importation, distribution, and sale of alcoholic beverages in the State of California. The ABC's mission is to administer the provisions of the Alcoholic Beverage Control Act in a manner that fosters and protects the health, safety, welfare, and economic well-being of the people of California.

The ABC receives funding from liquor license fees and escheated unclaimed checks or warrants. Its general operations are administered through the Alcoholic Beverage Control Fund (Fund 3036). ABC also administers federal grants. ABC passes through the federal grants to local law enforcement agencies to support various alcohol-related initiatives.

SCOPE

Pursuant to an interagency agreement with ABC, Finance conducted a review of the following:

- ABC's federal grant management and budgetary processes.
- Federal grant receipts and expenditures for fiscal years 2003-04 through 2007–08.
- Revenue and expenditure activity in Fund 3036 for fiscal years 2003-04 through 2007-08.
- ABC's fund condition statements and fund balance for fiscal years 2003-04 through 2007-08.

METHODOLOGY

We interviewed staff of the following: ABC; State Controller's Office (SCO); Department of Finance's Budget Operations, Fiscal Operations, CALSTARS, and Financial Services and Consulting Units. Topics discussed included:

- Federal grant management policies and procedures.
- Federal grant revenues and expenditures.
- Budgetary policies and procedures.
- Budgetary/legal basis financial reporting.
- Fund condition statement preparation.
- Fund 3036 revenues and expenditures.

To meet the review's objectives we performed the following steps:

- Quantified federal grant receipts and expenditures.
- Performed analytical reviews of federal grant receipts and expenditures.
- Reviewed documents supporting federal grant receipts and expenditures.
- Compared budgeted federal grant appropriations to actual expenditures.
- Reviewed documents supporting ABC's year-end SCO reports.
- Compared ABC's year-end SCO reports to fund condition statement amounts.
- Compared fund condition statement amounts to those presented in the Governor's Budget.
- Reviewed year-end journal entries and adjustments to the fund balance.
- Researched and resolved mispostings to the CALSTARS general ledger.

Recommendations were developed based on our review of documentation, observations, and interviews with the above mentioned staff.

The review was conducted during the period January 2009 through June 2009.

During our review, we identified a lack of sufficient supporting documentation for Fund 3036's fund condition statements reported in the Governor's Budget. Therefore, we reconstructed the statements for fiscal years 2003-04 through 2007-08 (Appendix A).

We also identified weaknesses in ABC's federal grant management and budgetary processes. Observations are presented in the following two categories:

- Fund 3036 Fund Condition Statements.
- Federal Grant Management and Budgetary Processes.

By implementing corrective actions for the observations described below, ABC can improve and strengthen its fiscal operations.

FUND 3036 FUND CONDITION STATEMENTS

The following observations were identified during our review of Fund 3036's fund condition statements and subsequent reconstruction.

Observation 1: Unsupported Fund Condition Statements

Our review disclosed material variances and insufficient support for the reported amounts of Fund 3036. The fund condition statements, as reported in the Governor's Budget for fiscal years 2004-05 through 2007-08, were not supported by ABC's year-end records or budget documents maintained by Finance's Business Transportation and Housing Unit (BT&H) (i.e. schedule 10s and 10Rs). As a result, we reconstructed the fund condition statements for 2003-04 through 2007-08 from ABC's year-end records which included CALSTARS and SCO reports. Upon reconstruction, we determined Fund 3036's ending fund balance for fiscal year 2007-08 was understated by approximately $2.2 million. The Governor's Budget reported $10.7 million, while our reconstruction demonstrated a balance of $12.9 million (Appendix A).

Recommendations:

1. Implement policies and procedures to ensure the fund condition statements are accurately prepared and supported.

2. Calculate and post a prior year-adjustment to correctly state the 2008-09 beginning fund balance as reported in the 2010-11 Governor's Budget.

Observation 2: Deficiencies Identified in ABC's Year-End Processes

Accruals identified in ABC's Report of Accruals for fiscal year 2006-07 and ABC's Final Reconciliation with SCO's Report (Report 15) did not agree. Variances identified in the year-end SCO reports were not supported by ABC's records, and could not be validated by

ABC. Although the variances impacted specific line item expenditures on Report 15; the aggregate expenditures were not impacted. Failure to maintain accurate balances could result in year-end reporting errors.

Recommendations:

3. Implement policies and procedures to ensure the accuracy of year-end reports.

4. Retain documentation supporting year-end report amounts and calculations.

Observation 3: Unsupported Year-End Adjusting Entries

Unsupported journal entries to Fund 3036's cash in state treasury account and fund balance were identified during reconstruction of the fund condition statements. Per discussion with ABC staff, these entries were posted to balance Fund 3036's cash accounts and to complete the fiscal year-end close. Validation of the entries could not be found in ABC's batch logs or fiscal records. The entries resulted in a decrease of $51,129 and $91,189 in 2005-06 and 2006-07 cash and fund balance, respectively. Due to the lack of support, these amounts are not included in the reconstructed statements presented in Appendix A.

Recommendations:

5. Post a correcting entry to CALSTARS to reverse the unsupported entries.

6. Implement policies and procedures requiring staff to research and resolve discrepancies in the accounting records or reports prior to calculating and posting adjusting entries.

7. Implement policies and procedures to review and approve journal entries to ensure accuracy and propriety. The approval should be by someone other than the preparer and performed prior to posting. Additionally, retain sufficient documentation to support the rationale for entries.

Observation 4: Bank Reconciliations Not Performed

The ABC has not performed bank reconciliations for its cash in state treasury bank account, as required by Section 7923 of the State Administrative Manual (SAM). During our review, ABC provided check and deposit listings; however, a complete reconciliation of the bank account had not been performed since July 2005. A cursory review identified a potential $36,432 variance. Completing timely reconciliations of the bank accounts ensures the accuracy of the fiscal reports and allows for timely research and resolution of variances. Preparing bank reconciliations is a fundamental accounting function essential for decreasing the risk for theft and financial misstatements.

Recommendations:

8. Immediately reconcile the cash in state treasury bank account and research and resolve variances identified.

9. Implement policies and procedures to reconcile cash in state treasury as required by SAM.

10. Implement polices and procedures for the review and approval of bank reconciliations by someone other than the preparer.

Observation 5: Inconsistent and Improper Recording of Expenditures

The ABC has not consistently recorded SCO 21st Century Project expenditures in CALSTARS, although the amounts directly reduced Fund 3036's balance. Since fiscal year 2004-05, SCO has prepared a plan of financial adjustment withdrawing funds from Fund 3036's cash in state treasury account. Upon withdrawal, SCO instructs ABC to post a journal entry in CALSTARS. When reviewing the 21st Century Project expenditures, we found that ABC did not consistently post the journal entries as illustrated in Table 1.

The SCO entries identified below are reflected in the proper fiscal year in the reconstructed fund condition statements presented in Appendix A.

Table 1
SCO 21st Century Project Fees
Fiscal Years 2004-05 through 2007-08

Fiscal Year	Amount	Posted
2004-05	$ 10,208	No
2005-06	32,500	Yes
2006-07	64,445	No
2007-08	72,659	No
Total	$ 179,812	

Recommendations:

11. Post all SCO journal entries to CALSTARS upon receipt.

12. Research and resolve any SCO entries that ABC is unclear about.

FEDERAL GRANT MANAGEMENT AND BUDGETARY PROCESSES

The following observations were identified during our review of ABC's federal grant management and budgetary processes.

Observation 6: No Documented Policies and Procedures

The ABC does not maintain written policies and procedures governing its federal grant management or budgetary processes. For example, ABC does not have documented policies and procedures for the following processes:

- Federal grant funding application.
- Federal fund receipt and monitoring.
- Federal fund expenditures.
- Federal fund draw-downs.
- Year-end closing.
- Fund condition statement preparation.
- Budget estimate preparation.
- Schedule 10 & 10R preparation.

- Budget revision preparation.
- Budget change proposal development.

Failure to adequately document and maintain current policies and procedures increases the risk of inconsistencies and errors within operational processes and fiscal records. This also diminishes the effectiveness of staff training should turnover occur.

Recommendation:

13. Document key federal grant management and budgetary processes. Periodically review and revise as deemed necessary to ensure current practices are reflected.

Observation 7: Key Person Dependency

A key person dependency exists within ABC's federal grant management and budgetary processes. One person is responsible for the following:

Federal Grant Management

- Entering expenditures into CALSTARS.
- Preparing invoices for reimbursement.
- Tracking and recording expenditures in subsidiary schedules.
- Performing the federal draw-down for reimbursement.

Budgetary

- Preparing year-end SCO reports.
- Preparing fund condition statements.
- Preparing budget estimates.
- Reviewing Schedule 10s and 10R's.
- Preparing budget revisions.
- Preparing budget change proposals.
- Preparing various other budget related submissions.

Combined with the lack of documented policies and procedures, relying on key staff could impact ABC's operational efficiency and effectiveness should staff turnover or absence occur.

Recommendation:

14. Cross-train ABC fiscal staff to ensure the above mentioned duties can be completed in the absence of key staff.

Observation 8: Inappropriate Expenditure of Federal Funds

The ABC did not obtain prior authority to receive and expend federal grant funds as required by SAM Section 0912. Specifically, up until 2005-06, the grants were received by the California Office of Traffic Safety (OTS) and transferred to ABC. Beginning in 2006, OTS informed the ABC that ABC would need to apply directly to the Federal Department of Justice (DOJ) for the grants. However, ABC did not recognize the necessity of notifying Finance's BT&H Unit until October 2007.

In October 2007, ABC requested Finance's BT&H unit to establish a Federal Trust Fund (Fund 0890) and increase its 2007-08 expenditure authority by $1.3 million, for receipt of four federal grants. At the time of the request, ABC had already been awarded $700,000 for two grants ($350,000 each) pertaining to fiscal years 2005-06 and 2006-07. Although ABC subsequently received approval from Finance for the 2007-08 federal grant funding, grant expenditures were inappropriately disbursed through Fund 3036's State Operations Appropriation as presented in Table 2.

Table 2
Fund 3036
Federal Grant Expenditures
Fiscal Years 2005-06 through 2007-08

Fiscal Year	2005-06	2006-07	2007-08	Total
Expenditures	$ 38,120	$560,020	$ 271,665	$869,805

Fund 0890 was established in 2008-09 and ABC indicated the expenditures inappropriately disbursed from Fund 3036 were transferred to this fund; however we did not verify this transfer. The expenditures shown in Table 2 are not included in the reconstructed statements presented in Appendix A.

Recommendations:

15. Implement policies and procedures to ensure guidelines set forth in SAM are known and implemented by staff.

16. Implement policies and procedures requiring appropriation authority to be received prior to expending or receiving additional federal grant funding.

17. Reimburse Fund 3036 for the improper expenditures as shown in Table 2.

18. Verify federal grant expenditures and reimbursements posted to Fund 3036 are transferred to Fund 0890.

Observation 9: Federal Grant Reimbursements Not Posted to CALSTARS

ABC did not timely post federal grant reimbursements received to CALSTARS. Through the federal draw-down process, ABC requests and receives quarterly reimbursements from DOJ for expenditures incurred. The ABC utilizes the draw-down process where reimbursements are directly remitted to ABC's bank account held with the State Treasurer's Office (STO). Once ABC receives confirmation that the funds have been deposited, a Remittance Advice is prepared and sent to notify SCO of the receipt. The SCO then generates a journal entry instructing ABC to post the activity to CALSTARS. Because ABC did not have a federal trust fund appropriation established, the journal entries were not recorded in CALSTARS. The following table depicts the reimbursements deposited into ABC's cash in state treasury account.

Table 3
Federal Grant Reimbursements
Fiscal Years 2005-06 through 2007-08

Fiscal Year	2005-06	2006-07	2007-08	Total
Reimbursements	$ 0	$ 396,839	$ 403,452	$ 800,291

Recommendations:

19. Post federal grant reimbursements held in the STO bank account to CALSTARS.

20. Implement policies and procedures requiring federal grant reimbursements to be timely posted to CALSTARS, Fund 0890.

Observation 10: Lack of Federal Grant Reconciliations

The ABC does not periodically perform reconciliations or second-level reviews of federal grant expenditures with reimbursements. As a result, a posting error went undetected by the ABC. Specifically, expenditures in the amount of $47,245 pertaining to the Beale Air Force Base federal grant were not recorded in the proper CALSTARS accounts. Although ABC corrected the error upon notification, by not periodically reconciling or performing second level reviews, material misstatements in the accounting records may occur and not be timely detected.

Recommendation:

21. Implement policies and procedures requiring periodic reconciliations of federal grant expenditures with reimbursements. Additionally, require the reconciliations to be reviewed for propriety and accuracy by someone other than the preparer.

Alcohol Beverage Control Fund (Fund 3036)
Reconstructed Fund Condition Statements

Dollars in Thousands

	2003-04	2004-05	2005-06	2006-07	2007-08
BEGINNING BALANCE		$ 5,724	$ 11,376	$ 13,995	$ 13,473
Prior Year Adjustments	$ (25)	(32)	(111)	(482)	2,099
Adjusted Beginning Balance	(25)	5,692	11,265	13,513	15,572
REVENUES, TRANSFERS, AND OTHER ADJUSTMENTS					
Revenues:					
12100 Liquor License Fees	41,200	44,975	45,534	48,477	47,384
161000 Escheat Unclaimed Checks & Warrants	30	36	51	101	103
161400 Miscellaneous Revenue	6	5	5	5	52
Transfers and Other Adjustments					
FO0081 From Alcohol Beverage Control Fund	3,710	1,510	0	27	
Refunds to Reverted Appropriations		0			0
FO00683 Operating transfers in		83			93
Total Revenues, Transfers, and Other Adjustments	44,946	46,609	45,590	48,610	47,632
Total Resources	44,921	52,301	56,855	62,123	63,204
EXPENDITURES AND EXPENDITURE ADJUSTMENTS					
Expenditures:					
0840 State Controller (State Operations)	0	10	33	64	73
2100 Department of Alcoholic Beverage Control					
State Operations	37,697	39,419	41,327	45,588	47,390
Local Assistance	1,500	1,496	1,500	2,998	2,771
9670 equity Claims of CA Victim Compensation Bd.	0				
Total Expenditures and Expenditure Adjustments	39,197	40,925	42,860	48,650	50,234
FUND BALANCE	$ 5,724	$11,376	$ 13,995	$ 13,473	$ 12,970
Immaterial Variances[1]					19
ADJUSTED FUND BALANCE					$ 12,989

[1] Variances were identified during reconstruction of the fund condition statement that are deemed immaterial as they are less than 1 percent of the fund balance.

Attachment referenced on page 18 excluded from final report—duplicates information in Appendix A.

Memorandum

To: Dave Botelho, Chief
Department of Finance
Office of State Audits and Evaluations
915 L Street
Sacramento, CA 95814-3706

Date: October 8, 2009

From: **Department of Alcoholic Beverage Control**
Director's Office
3927 Lennane Drive, Suite 100
Sacramento, CA 95834

Subject: **Special Review – Department of Alcoholic Beverage Control**

This will serve as the Department of Alcoholic Beverage Control's (ABC) response to the findings and recommendations made by the Office of State Audits and Evaluations in their Special Review dated June 2009.

I wish to extend my thanks to you and your staff for conducting this review. We believe that as a result of this review ABC has or will have in place the proper policies, procedures and control mechanisms to address your findings and recommendations.

FUND 3036 FUND CONDITION STATEMENTS

Observation 1: Unsupported Fund Condition Statements

The review disclosed material variances and insufficient support for the reported amounts of Fund 3036. The fund condition statements, as reported in the Governor's Budget for fiscal years 2004-05 through 2007-08, were not supported by year-end records or budget documents maintained by Finance's Budget Operations (i.e. Schedule 10s and 10Rs). As a result, we reconstructed the fund condition statements for 2003-04 through 2007-08 from ABC's year-end records which included CALSTARS and SCO reports. Upon reconstruction, the review determined Fund 3036's ending fund balance for fiscal year 2007-08 was understated by approximately $2.2 million. The Governor's Budget reported $10.7 million, while the reconstruction demonstrated a balance of $12.9 million.

Recommendations:

1. Implement policies and procedures to ensure the fund condition statements are accurately prepared and supported.
2. Calculate and post a prior-year adjustment to correctly state the 2008-09 beginning fund balance as reported in the 2010-11 Governor's Budget.

Response to Recommendations

We concur. The Department has already put in place the required internal procedures to ensure the proper and accurate reporting of revenue and expenditure data to its fund condition statements. Additionally, the Department has already calculated and submitted a year-end adjustment to correctly state the 2008-09 beginning fund balance, although the adjustment is $497,000 less than the approximately $2.2 million adjustment suggested by the Department of Finance's Office of State Audits and Evaluations. The year-end adjustment amount was reduced by $497,000 to reflect the amount that remains at the State Controllers' Office (SCO) with no mechanism to be transferred to the Department. The Department plans to seek additional guidance from the Department of Finance's Budget Operations before finalizing the FY 2010-11 budget.

Corrective action fully implemented.

Observation 2: Deficiencies Identified in ABC's Year-End Processes

Accruals identified in ABC's Report of Accruals for fiscal year 2006-07 and ABC's Final Reconciliation with SCO's Report (Report 15) did not agree. Variances identified in the year-end SCO reports were not supported by ABC's records, and could not be validated by ABC. Although the variances impacted specific line item expenditures on Report 15, the aggregate expenditures were not impacted. Failure to maintain accurate balances could result in year-end reporting errors.

Recommendations:

3. Implement policies and procedures to ensure the accuracy of year-end reports.
4. Retain documentation supporting year-end report amounts and calculations.

Response to Recommendations

We concur. The Department has already implemented policies and procedures to ensure the accuracy of year-end reports. In addition, the Department has designated a central location to store all documentation supporting year-end reports. Moreover, the Department requires staff involved in the year-end process to attend the annual year-end training offered by the Department of Finance, CalSTARS unit.

Corrective actions fully implemented.

Observation 3: Unsupported Year-End Adjusting Entries

Unsupported journal entries to Fund 3036's fund in state treasury account and fund balance were identified during reconstruction of the fund condition statements. Validation of the entries could not be found in ABC's batch logs or fiscal records. The entries resulted in a decrease of $51,129 and $91,189 in 2005-06 and 2006-07 cash and fund balance, respectively. Due to the lack of support, these amounts are not included in the reconstructed statements presented in Appendix A.

Recommendations:

5. Post a correcting entry to CALSTARS to reverse the unsupported entries.
6. Implement policies and procedures requiring staff to research and resolve discrepancies in the accounting records or reports prior to calculating and posting adjusting entries.
7. Implement policies and procedures to review and approve journal entries to ensure accuracy and propriety. The approval should be by someone other than the preparer and performed prior to posting. Additionally, retain sufficient documentation to support the rationale for entries.

Response to Recommendations:

We concur. The Department will post correcting entries in CalSTARS to reverse the unsupported entries in Fiscal Month 04. In addition, the Department has established policies and procedures to ensure proper posting of transactions. Furthermore, staff has been instructed to submit complex adjusting entries to the Accounting Officer for review and validation prior to posting.

Corrective actions fully implemented.

Observation 4: Bank Reconciliations Not Performed

ABC has not performed bank reconciliations for its cash in state treasury bank account as required by Section 7923 of the State Administrative Manual (SAM). A cursory review identified a potential $36,432 variance.

Recommendations:

8. Immediately reconcile the cash in state treasury bank account and research and resolve variances identified.
9. Implement policies and procedures to reconcile cash in state treasury as required by SAM.
10. Implement policies and procedures for the review and approval of bank reconciliations by someone other than the preparer.

Response to Recommendations

We concur. The Department has implemented policies and procedures to ensure the bank reconciliation is performed as required by SAM, Section 7923. The bank reconciliations are now performed monthly to ensure accuracy and reliability of financial data and all discrepancies are researched and rectified within a timely manner. Upon completion, the bank reconciliations are submitted to the Fiscal Officer for review and approval.

Corrective actions fully implemented.

Observation 5: Inconsistent and Improper Recording of Expenditures

ABC has not consistently recorded SCO 21st Century Project expenditures in CALSTARS, although the amounts directly reduced Fund 3036's balance.

Recommendations:

11. Post all SCO journal entries to CALSTARS upon receipt.
12. Research and resolve any SCO entries that ABC is unclear about.

Response to Recommendations

We concur. The Department has implemented new procedures to ensure all future journal entries received from SCO are processed upon receipt. In addition, the Department has identified all journal entries (past and present) relating to the 21st Century project expenditures. These journal entries have been posted accordingly in CalSTARS.

Corrective actions fully implemented.

FEDERAL GRANT MANAGEMENT AND BUDGETARY PROCESSES

Observation 6: No Documented Policies and Procedures

ABC does not maintain written policies and procedures governing its federal grant management or budgetary processes.

Recommendation:

13. Document key federal grant management and budgetary processes. Periodically review and revise as deemed necessary to ensure current practices are reflected.

Response to Recommendation

We concur. The Department has documented and implemented internal procedures for the Federal Grant Programs.

Corrective actions fully implemented.

Observation 7: Key Person Dependency

A key person exists within ABC's federal grant management and budgetary processes. Combined with the lack of documented policies and procedures, relying on key staff could impact ABC's operational efficiency and effectiveness should staff turnover or absences occur.

Recommendation:

14. Cross-train ABC fiscal staff to ensure the above mentioned duties can be completed in the absence of key staff.

Response to Recommendation

We concur. The Department has developed the required desk manuals to ensure day-to-day operations are not compromised in the event of staff absences or turnovers occur. Fiscal staff are currently being trained on federal grant management and budgetary processes to avoid such dependency.

Planned completion for corrective actions by June 30, 2010.

Observation 8: Inappropriate Expenditure of Federal Funds

ABC did not obtain prior authority to receive and expend federal grant funds as required by Section 0912 of the SAM. Specifically, up until 2005-06, the grants were received by the California Office of Traffic Safety (OTS) and transferred to ABC. Beginning in 2006, OTS informed ABC that ABC would need to apply directly to the Federal Department of Justice (DOJ) for the grants. However, ABC did not recognize the necessity of notifying Finance Budget Operations until October 2007. Fund 0890 was established in 2008-09 and ABC indicated the expenditures inappropriately disbursed from Fund 3036 were transferred to this fund; however we did not verify this transfer.

Recommendations:

15. Implement policies and procedures to ensure guidelines set forth in SAM are known and implemented by staff.

16. Implement policies and procedures requiring appropriation authority to be received prior to expending or receiving additional federal grant funding.
17. Reimburse Fund 3036 for the improper expenditures.
18. Verify federal grant expenditures and reimbursements posted to Fund 3036 are transferred to Fund 0890.

Response to Recommendations

We concur. Internal procedures have been implemented to ensure the Department is in compliance with SAM, Section 0912. Responsible staff are aware of the required guidelines set forth in SAM. Expenditures disbursed from Fund 3036 have been reversed and charged to Fund 0890 for Fiscal Year 2007-08. Appropriation authority is still pending resolution for Fiscal Years 2005-06 and 2006-07.

Corrective action with regard to reversal of expenditures has been implemented.

Planned completion for corrective action with regard to appropriation authority resolution must be completed by June 30, 2010.

Observation 9: Federal Grant Reimbursement Not Posted to CALSTARS

ABC did not timely post federal grant reimbursements received to CALSTARS. Because ABC did not have a federal trust fund appropriation established, the journal entries were not recorded in CALSTARS.

Recommendations:

19. Post federal grant reimbursements held in the SCO bank account to CALSTARS.
20. Implement policies and procedures requiring federal grant reimbursements to be timely posted to CALSTARS, Fund 0890.

Response to Recommendations

We concur. All journal entries (past and present) pertaining to the Federal Grants have been posted into CalSTARS. In addition, internal procedures have been documented and implemented to ensure future journal entries are processed timely. Furthermore, the Department has established procedures to reconcile Fund 0890 monthly.

Corrective actions fully implemented.

Observation 10: Lack of Federal Grant Reconciliations

ABC does not periodically perform reconciliations or second level reviews of federal grant expenditures with reimbursements. As a result, a posting error went undetected by the ABC. Specifically, expenditures in the amount of $47,245 pertaining to the Beale Air Force Base federal grant were not recorded in the proper CALSTARS accounts. Although ABC corrected the error upon notification, by not periodically reconciling or performing second level reviews, material misstatements in the accounting records may occur and not be timely detected.

Recommendation:

21. Implement policies and procedures requiring periodic reconciliations of federal grant expenditures with reimbursements. Additionally, require the reconciliations to be reviewed for propriety and accuracy by someone other than the preparer.

Response to Recommendation

We concur. The Department has assigned the task of reconciling Fund 0890 to staff. Additionally, the Department has implemented procedures to ensure reconciliations are performed on a timely basis and all identified discrepancies corrected in a timely manner in order to reduce the risks of misstatements. Upon completion, the Federal Grant reconciliation will be submitted to the Fiscal Officer for review and approval.

Corrective actions fully implemented.

If you have questions or require further information concerning our response, please contact Ed Jimenez, Assistant Director Administration at (916) 419-2511 or email at Ed.Jimenez@abc.ca.gov.

Stephen M. Hardy
Director

Attachment: Appendix A

EVALUATION OF RESPONSE

We have reviewed ABC's response, dated October 8, 2009 to our draft audit report. The Attachment referenced in the response has been omitted in the interest of brevity. The ABC generally concurred with our observations.

We commend ABC on its prompt action to improve the administrative oversight and operations of its grant programs and acknowledge the implementation of corrective actions to resolve the observations noted in our report. In evaluating ABC's response, we provide the following comments:

With respect to Observations 1 and 8, the ABC concurred with our recommendations, but noted that it could not fully implement the recommendations proposed. Specifically, ABC reduced the recommended $2.2 million adjustment by $497,000 because it currently has no mechanism to reimburse Fund 3036 for the federal grant expenditures incurred prior to its appropriation authority.

Although federal reimbursements have been received for the grant expenditures—and are being held in the State Treasury—because the ABC does not have federal grant appropriation authority for 2005-06 and 2006-07, the federal reimbursements received cannot be transferred into Fund 3036.

Legislation is necessary to provide the necessary appropriation authority for the federal grants received in 2005-06 and 2006-07. If legislation is not passed by June 2010, ABC will have no recourse but to have Fund 3036 absorb the unreimbursed expenditures, thereby reducing the fund balance as reported in Appendix A by $497,000.