



# MICHIGAN

OFFICE OF THE AUDITOR GENERAL

## AUDIT REPORT



THOMAS H. MCTAVISH, C.P.A.  
AUDITOR GENERAL

The auditor general shall conduct post audits of financial transactions and accounts of the state and of all branches, departments, offices, boards, commissions, agencies, authorities and institutions of the state established by this constitution or by law, and performance post audits thereof.

– Article IV, Section 53 of the Michigan Constitution

Audit report information can be accessed at:

*<http://audgen.michigan.gov>*



Michigan  
Office of the Auditor General  
**REPORT SUMMARY**

**Financial Audit**

*Including the Provisions of the Single Audit Act*

Report Number:  
511-0100-12

**Department of Military and Veterans Affairs**

*October 1, 2009 through September 30, 2011*

Released:  
June 2012

*A single audit is designed to meet the needs of all financial report users, including an entity's federal grantor agencies. The audit determines if the financial schedules and/or financial statements are fairly presented; considers internal control over financial reporting and internal control over federal program compliance; determines compliance with requirements material to the financial schedules and/or financial statements; and assesses compliance with direct and material requirements of the major federal programs.*

**Financial Statements:**

**Auditor's Report Issued**

We issued an unqualified opinion on the Department of Military and Veterans Affairs' (DMVA's) financial statements.

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**Internal Control Over Financial Reporting**

We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses. However, we did identify significant deficiencies (Findings 1 through 5).

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**Noncompliance and Other Matters  
Material to the Financial Statements**

We did not identify any instances of noncompliance or other matters applicable to the financial statements that are required to be reported under *Government Auditing Standards*. However, we did identify other noncompliance (Findings 2 through 5).

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**Federal Awards:**

**Auditor's Reports Issued on Compliance**

We audited 4 programs (including 1 ARRA related program) as major programs and identified known questioned costs of \$7.6 million. DMVA expended a total of \$200.6 million in federal awards, including \$11.1 million of ARRA funding, during the two-year period ended September 30, 2011. We issued 3 unqualified opinions and 1 adverse opinion. The opinions issued by major program are identified on the back of this summary.

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**Internal Control Over Major Programs**

We identified material weaknesses in internal control over federal program compliance (Finding 8). We also identified significant deficiencies in internal control over federal program compliance (Findings 6 through 8).

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**Required Reporting of Noncompliance**

We identified instances of noncompliance that are required to be reported in accordance with U.S. Office of Management and Budget (OMB) Circular A-133 (Findings 6 through 8).

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**Internal Accounting and Administrative Control System:**

Section 18.1489 of the *Michigan Compiled Laws* requires the Auditor General to evaluate the implementation of Sections 18.1483 - 18.1488 of the *Michigan Compiled Laws* and report to the Legislature in the financial audit of each department. As a result of Executive Reorganization Order No. 2007-31 (Consolidating Internal Audit Functions), in which responsibility for most of the sections was moved to the Office of Internal Audit Services, State Budget Office, we have evaluated the implementation of only Section 18.1485 in this financial audit. Section 18.1485 requires each department director to

establish an internal accounting and administrative control system, defines the elements of that system, defines the duties of the department director, and provides for certain reports. We determined that DMVA was in substantial compliance with Section 18.1485 of the *Michigan Compiled Laws*.

The remaining sections (Sections 18.1483, 18.1484, and 18.1486 - 18.1488 of the *Michigan Compiled Laws*) will be evaluated and reported on in the performance audit of the Office of Internal Audit Services, State Budget Office.

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We audited the following programs as major programs:

<u>CFDA Number</u>	<u>Program Title</u>	<u>Compliance Opinion</u>
12.400	Military Construction, National Guard	Unqualified
12.401	<u>National Guard Military Operations and Maintenance (O&amp;M) Projects:</u> <ul style="list-style-type: none"> <li>• National Guard Military Operations and Maintenance (O&amp;M) Projects</li> <li>• ARRA - National Guard Military Operations and Maintenance (O&amp;M) Projects</li> </ul>	Unqualified
12.404	National Guard ChalleNGe Program	Adverse
64.015	Veterans State Nursing Home Care	Unqualified

A copy of the full report can be obtained by calling 517.334.8050 or by visiting our Web site at: <http://audgen.michigan.gov>



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Lansing, Michigan 48913

**Thomas H. McTavish, C.P.A.**  
Auditor General

**Scott M. Strong, C.P.A., C.I.A.**  
Deputy Auditor General



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THOMAS H. MCTAVISH, C.P.A.  
AUDITOR GENERAL

June 21, 2012

Major General Gregory J. Vadnais, Director  
Department of Military and Veterans Affairs  
3411 North Martin Luther King Jr. Boulevard  
Lansing, Michigan

Dear General Vadnais:

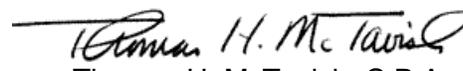
This is our report on the financial audit, including the provisions of the Single Audit Act, of the Department of Military and Veterans Affairs (DMVA) for the period October 1, 2009 through September 30, 2011.

This report contains our report summary; our independent auditor's report on the financial statements; and DMVA's financial statements, statement of certain General Fund assets and liabilities, and schedule of expenditures of federal awards. This report also contains our independent auditor's report on internal control over financial reporting and on compliance and other matters, our independent auditor's report on compliance with requirements that could have a direct and material effect on each major program and on internal control over compliance in accordance with U.S. Office of Management and Budget Circular A-133, and our schedule of findings and questioned costs. In addition, this report contains DMVA's summary schedule of prior audit findings, its corrective action plan, and a glossary of acronyms and terms.

Our findings and recommendation are contained in Section II and Section III of the schedule of findings and questioned costs. The agency preliminary responses are contained in the corrective action plan. The *Michigan Compiled Laws* and administrative procedures require that the audited agency develop a plan to comply with the audit recommendations and submit it within 60 days after release of the audit report to the Office of Internal Audit Services, State Budget Office. Within 30 days of receipt, the Office of Internal Audit Services is required to review the plan and either accept the plan as final or contact the agency to take additional steps to finalize the plan.

We appreciate the courtesy and cooperation extended to us during this audit.

Sincerely,

  
Thomas H. McTavish, C.P.A.  
Auditor General



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INDEPENDENT AUDITOR'S REPORT AND  
FINANCIAL STATEMENTS



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THOMAS H. MCTAVISH, C.P.A.  
AUDITOR GENERAL

## Independent Auditor's Report on the Financial Statements

Major General Gregory J. Vadnais, Director  
Department of Military and Veterans Affairs  
3411 North Martin Luther King Jr. Boulevard  
Lansing, Michigan

Dear General Vadnais:

We have audited the accompanying financial statements of the Department of Military and Veterans Affairs for the fiscal years ended September 30, 2011 and September 30, 2010, as identified in the table of contents. These financial statements are the responsibility of the Department's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1, the financial statements present only the sources and disposition of authorizations and the revenues and other financing sources of the Department of Military and Veterans Affairs' General Fund accounts, presented using the current financial resources measurement focus and the modified accrual basis of accounting. Accordingly, these financial statements do not purport to, and do not, constitute a complete financial presentation of the State's General Fund in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the sources and disposition of authorizations and the revenues and other financing sources of the Department of Military and Veterans Affairs for the fiscal years ended September 30, 2011 and September 30, 2010 on the basis of accounting described in Note 1.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 11, 2012 on our consideration of the Department's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The schedule of expenditures of federal awards, required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and the statement of certain General Fund assets and liabilities are presented for purposes of additional analysis and are not a required part of the Department's financial statements referred to in the first paragraph. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

Sincerely,

  
Thomas H. McTavish, C.P.A.  
Auditor General  
June 11, 2012

DEPARTMENT OF MILITARY AND VETERANS AFFAIRS  
Statement of Sources and Disposition of General Fund Authorizations  
Fiscal Years Ended September 30

	<u>2011</u>	<u>2010</u>
<b>SOURCES OF AUTHORIZATIONS (Note 2)</b>		
General purpose appropriations	\$ 35,985,500	\$ 36,245,000
Balances carried forward	4,151,659	2,279,932
Restricted financing sources	103,119,910	123,233,949
Less: Intrafund expenditure reimbursement	(662,688)	(527,374)
Total sources of authorizations	<u>\$ 142,594,381</u>	<u>\$ 161,231,507</u>
<b>DISPOSITION OF AUTHORIZATIONS (Note 2)</b>		
Gross expenditures and transfers	\$ 124,500,175	\$ 129,986,711
Capital outlay	13,711,708	26,694,945
Less: Intrafund expenditure reimbursement	(662,688)	(527,374)
Net expenditures and transfers	<u>\$ 137,549,195</u>	<u>\$ 156,154,282</u>
Gross authorizations for carry forward	\$ 5,045,186	\$ 5,077,226
Balances lapsed	(573,061)	(925,567)
Net authorizations carried forward	<u>\$ 4,472,125</u>	<u>\$ 4,151,659</u>
Balances carried forward:		
Encumbrances	\$ 379,918	\$ 418,536
Restricted revenues - authorized		
Restricted revenues - not authorized or used	3,915,039	3,544,763
Multi-year projects	177,168	188,360
Total balances carried forward	<u>\$ 4,472,125</u>	<u>\$ 4,151,659</u>

The accompanying notes are an integral part of the financial statements.

DEPARTMENT OF MILITARY AND VETERANS AFFAIRS  
Statement of General Fund Revenues and Other Financing Sources  
Fiscal Years Ended September 30

	<u>2011</u>	<u>2010</u>
<b>REVENUES</b>		
From federal agencies:		
National Guard Bureau	\$ 52,818,055	\$ 70,207,564
Veterans Administration State Home Program	26,725,116	28,145,931
Medicare and Medicaid	2,606,479	2,767,433
U.S. Department of Justice	181,896	39,277
U.S. Department of Health and Human Services	90,000	100,000
Total from federal agencies	<u>\$ 82,421,546</u>	<u>\$ 101,260,205</u>
From local agencies:		
Local School Aid Fund (Note 4)	\$ 805,948	\$ 740,079
Total from local agencies	<u>\$ 805,948</u>	<u>\$ 740,079</u>
From services:		
Cost-of-care assessments	\$ 18,648,333	\$ 20,029,907
Mackinac Bridgewalk	51,212	53,035
Other services	291,411	320,659
Total from services	<u>\$ 18,990,956</u>	<u>\$ 20,403,601</u>
Miscellaneous revenue:		
Miscellaneous	\$ 125,151	\$ 110,325
Armory Rental Program	85,766	93,762
Total miscellaneous revenue	<u>\$ 210,917</u>	<u>\$ 204,087</u>
Total revenues	<u>\$ 102,429,367</u>	<u>\$ 122,607,972</u>
<b>OTHER FINANCING SOURCES</b>		
Proceeds from sale of capital assets - Armory sales	<u>54,200</u>	<u>200,000</u>
Total revenues and other financing sources	<u><u>\$ 102,483,567</u></u>	<u><u>\$ 122,807,972</u></u>

The accompanying notes are an integral part of the financial statements.

## Notes to the Financial Statements

### Note 1 Significant Accounting Policies

#### a. Reporting Entity

The accompanying financial statements report the results of the Department of Military and Veterans Affairs' (DMVA's) General Fund financial transactions for the fiscal years ended September 30, 2011 and September 30, 2010. DMVA is one of 17 departments that record their activities in the General Fund. The General Fund is reported on in the *State of Michigan Comprehensive Annual Financial Report (SOMCAFR)*.

In addition to its General Fund activities, DMVA is also responsible for the supervision and direction of the Michigan Veterans' Trust Fund (a permanent fund) and the Military Family Relief Fund (a special revenue fund). Because these funds do not receive federal funding, they are not included in the scope of this audit.

The notes accompanying these financial statements relate directly to DMVA. The *SOMCAFR* provides more extensive disclosures regarding the State's significant accounting policies; budgeting, budgetary control, and legal compliance; pension benefits; other postemployment benefits; and compensated absences.

#### b. Measurement Focus, Basis of Accounting, and Presentation

The financial statements contained in this report are presented using the current financial resources measurement focus and the modified accrual basis of accounting, as provided by accounting principles generally accepted in the United States of America (GAAP). Under the modified accrual basis of accounting, revenues are recognized as they become susceptible to accrual, generally when they are both measurable and available. Revenues are considered to be available when they are collected within the current period or soon enough thereafter to pay liabilities of the current period. Expenditures generally are recorded when a liability is incurred; however, certain expenditures related to long-term obligations are recorded only when payment is due and payable.

Because DMVA is part of the State's General Fund, these financial statements do not purport to, and do not, constitute a complete financial presentation of the State's General Fund in conformity with GAAP. Because the Governmental Accounting Standards Board (GASB) has not established specific accounting and reporting standards for the reporting of less than a complete fund, DMVA, in conjunction with the Department of Technology, Management, and Budget, based on guidance provided in the American Institute of Certified Public Accountants (AICPA) Audit and Accounting Guide for State and Local Governments, has developed the statement of sources and disposition of General Fund authorizations. DMVA believes that this statement best represents the results of DMVA's operations (reflected on the gross authorizations for carry forward line) and DMVA's financial position (reflected on the net authorizations carried forward line).

The resources available to DMVA and how those resources may be used are established through the legislative appropriation process. Consequently, the statement of sources and disposition of General Fund authorizations is very similar to an operating statement. The statement reports the resources available to DMVA for its General Fund operations: general purpose appropriations (from the general resources of the General Fund), authorization balances carried forward from the prior fiscal year, and restricted financing sources (revenue collected by DMVA in the performance of its responsibilities). The statement also reports how those resources were used and what balance is available to DMVA in the next fiscal year (similar to fund balance).

The statement of General Fund revenues and other financing sources provides information regarding DMVA's collections of restricted revenue and other financing sources generated from DMVA's operations.

DMVA has included a statement of certain General Fund assets and liabilities as supplemental information. The statement reports only those assets and liabilities that are the responsibility of DMVA.

In accordance with GAAP, amounts expended by DMVA in the acquisition of capital assets are reported as capital outlay expenditures. The corresponding asset acquired is reported in the *SOMCAFR* on the government-wide financial statements. Under the modified accrual basis of accounting, capital assets are not reported in governmental funds. Note 6 provides information on those capital assets that are the responsibility of DMVA.

In addition, the notes include various disclosures that provide information about liabilities of a long-term nature that are not reported in governmental funds under the modified accrual basis of accounting (see Note 5, Military Retirement Benefits; Note 7, Compensated Absences; Note 8, Pension Benefits; Note 9, Other Postemployment Benefits; and Note 10, Risk Management).

Note 2 Statement of Sources and Disposition of General Fund Authorizations

The various elements of the statement of sources and disposition of General Fund authorizations are defined as follows:

- a. General purpose appropriations: Original appropriations and any supplemental appropriations that are financed by General Fund/general purpose revenues.
- b. Balances carried forward: Authorizations for multi-year projects, encumbrances, restricted revenues - authorized, and restricted revenues - not authorized or used that were not spent as of the end of the prior fiscal year. These authorizations are available for expenditure in the current fiscal year for the purpose of the carry-forward without additional legislative authorization, except for the restricted revenues - not authorized or used. In addition to the amount recorded in the financial statements, DMVA also has spending authorization available for large capital outlay projects that will be primarily financed through the collection of future federal revenue. Because the federal revenue has not yet been earned or received, the spending authorizations are not included on the statement of sources and dispositions of General Fund authorizations. The total amount of the spending authorizations was \$93,182,100 for fiscal year 2010-11 and \$106,750,455 for fiscal year 2009-10.

- c. Restricted financing sources: Collections of restricted revenues, restricted transfers, and restricted intrafund expenditure reimbursements used to finance programs as detailed in the appropriations act. These financing sources are authorized for expenditure up to the amount appropriated. Depending upon program statute, any amounts received in excess of the appropriation are, at year-end, either converted to general purpose financing sources and made available for general appropriation in the next fiscal year or carried forward to the next fiscal year as either restricted revenues - authorized or restricted revenues - not authorized or used. DMVA's restricted financing sources include federal revenue, cost-of-care assessments, and local revenue for the National Guard Challenge Program (Note 4).
- d. Intrafund expenditure reimbursement: DMVA provided services to the Michigan Department of State Police for U.S. Department of Homeland Security grants. Because both departments are in the General Fund, DMVA recorded the reimbursement received as an expenditure credit.
- e. Balances lapsed: Authorizations that were unexpended and unobligated at the end of the fiscal year. These amounts are available for legislative appropriation in the subsequent fiscal year.
- f. Encumbrances: Authorizations carried forward to finance payments for goods or services ordered during the fiscal year but not received by fiscal year-end. These authorizations are generally limited to obligations funded by general purpose appropriations.
- g. Restricted revenues - authorized: Revenues that, by statute or the Michigan Constitution, are restricted and authorized for use to a particular program or activity. Generally, these revenue carry-forwards may be expended for the purpose of the carry-forwards without additional legislative authorization.
- h. Restricted revenues - not authorized or used: Revenues that, by statute, are restricted for use to a particular program or activity. Generally, the expenditure of the restricted revenues is subject to annual legislative

appropriation. In fiscal year 2010-11, significant carry-forwards of this type included federal assistance of \$2,558,123 from the U.S. Department of Veterans Affairs, \$21,515 in cost-of-care assessments collected by the Grand Rapids Home for Veterans and the D.J. Jacobetti Home for Veterans, \$1,033,870 for the Michigan National Guard Armory Construction Fund (Note 3), and \$301,530 for the Michigan Youth ChalleNGe Academy. In fiscal year 2009-10, significant carry-forwards included federal assistance of \$2,358,045 from the U.S. Department of Veterans Affairs, \$91,770 in cost-of-care assessments collected by the Grand Rapids Home for Veterans and the D.J. Jacobetti Home for Veterans, \$1,012,780 for the Michigan National Guard Armory Construction Fund (Note 3), and \$82,022 for the Michigan Youth ChalleNGe Academy.

- i. Multi-year projects: Unexpended authorizations for work projects and capital outlay projects, financed with general purpose authorizations, that are carried forward to subsequent fiscal years for the completion of the projects. DMVA carried forward amounts for special maintenance, remodeling, and additions of \$177,168 in fiscal year 2010-11 and \$188,360 in fiscal year 2009-10.

Note 3 Michigan National Guard Armory Construction Fund

Act 150, P.A. 1967, created the Michigan National Guard Armory Construction Fund as a subfund of the General Fund. The proceeds from the sale of capital assets (land and armories) and interest earnings are deposited in the Fund and restricted for use in funding State armory capital outlay projects. The balance of the Fund was \$1,033,870 at September 30, 2011 and \$1,012,780 at September 30, 2010. DMVA had additions to the Fund of \$58,328 in fiscal year 2010-11 and \$205,727 in fiscal year 2009-10. DMVA used \$37,237 in fiscal year 2010-11 and \$110,385 in fiscal year 2009-10.

Note 4 National Guard ChalleNGe (NGC) Program

The NGC Program is for high school dropouts aged 16 to 18 upon entry. The goal of the Program is to use the National Guard to improve education, life skills, and employment potential of participants by use of military-based training and supervised work experience. The Program is administered by DMVA and

funded in part with federal funds requiring a 40% match in fiscal year 2009-10 and a 25% match in fiscal year 2010-11, which is provided from the School Aid Fund through the Battle Creek Public School District.

As required by Section 24c of both Act 204, P.A. 2010, and Act 121, P.A. 2009, DMVA has entered into a contract with the Battle Creek Public School District that outlines the terms and conditions upon which the District will utilize the Program funding. In summary, the Battle Creek Public School District received a distribution from the School Aid Fund of \$742,300 for fiscal year 2010-11 and \$642,300 for fiscal year 2009-10. The contract directs the District to request, receive, and deposit these funds in the District's checking account and then, using a check drawn on the District's checking account, to return these funds to DMVA. DMVA reports these funds as local revenue. The contract further requires DMVA to utilize all funds received from the District to provide the State's match requirement for the NGC Program.

Note 5 Military Retirement Benefits

DMVA received annual appropriations for military retirement benefits for the Michigan National Guard members and special duty officers. These appropriations are made from the General Fund on a pay-as-you-go basis. Except for 23 special duty members, retirants receive \$600 in annual pension benefits.

Expenditures for the military retirement plan totaled \$3,709,285 for fiscal year 2010-11 and \$3,612,800 for fiscal year 2009-10. The actuarially determined unfunded liabilities (performed biennially) for the military retirement plan as of September 30, 2011 totaled \$77.3 million. The *SOMCAFR* provides more extensive disclosures regarding the military retirement plan.

Note 6 Capital Assets

Capital assets, which include land, buildings, and equipment, are reported at historical cost or, if donated, at the estimated fair market value at the date of acquisition. In some instances, capital asset historical costs were not available; therefore, the costs of these assets at the dates of acquisition have been estimated.

Capitalization policies: All land and nondepreciable land improvements are capitalized, regardless of cost. Equipment is capitalized when the cost of individual items exceeds \$5,000, and all other capital assets are capitalized when the cost of individual items or projects exceeds \$100,000.

The costs of normal maintenance and repairs that do not add to the value of assets or materially extend assets' lives are not capitalized.

The amounts reported for capital assets have not been reduced for accumulated depreciation. Depreciation is recorded under the accrual basis of accounting and is reported in the State's government-wide financial statements. Information on the State's depreciation policies is available in the *SOMCAFR*. The amounts reported for capital assets for the fiscal years ended September 30, 2010 and September 30, 2011 were:

	Balance at September 30, 2010	Additions	Deletions/ Adjustments	Balance at September 30, 2011
Land	\$ 9,949,348	\$ 551,864	\$ (45,375)	\$ 10,455,837
Buildings	257,347,305	7,335,806	(1,446,373)	263,236,738
Construction in progress	21,612,197	4,209,927	4,005,964	29,828,087
Equipment	7,246,399	449,550	(49,565)	7,646,384
<b>Total</b>	<b>\$296,155,249</b>	<b>\$12,547,147</b>	<b>\$ 2,464,651</b>	<b>\$311,167,046</b>

	Balance at September 30, 2009	Additions	Deletions/ Adjustments	Balance at September 30, 2010
Land	\$ 9,833,544	\$ 174,592	\$ (58,788)	\$ 9,949,348
Buildings	241,201,847	16,284,240	(138,782)	257,347,305
Construction in progress	14,814,244	14,386,612	(7,588,659)	21,612,197
Equipment	6,729,218	768,096	(250,915)	7,246,399
<b>Total</b>	<b>\$272,578,853</b>	<b>\$31,613,540</b>	<b>\$(8,037,144)</b>	<b>\$296,155,249</b>

**Note 7 Compensated Absences**

Employees accumulate annual leave (vacation) balances to maximum amounts ranging from 296 to 356 hours. The maximum accumulation that may be paid off is 40 hours less than the total hours that may be accumulated. Employees receive 100% termination payment upon separation based upon their final rate

of pay. The liability for annual leave is recorded at the maximum accumulation amounts in accordance with GAAP, as it is probable that the State will compensate employees through paid time off for the hours earned in excess of the total that may be paid off. The liability for annual leave is valued at 100% of the balance plus the State's share of social security and retirement contributions.

Employee sick leave balances accumulate without limit. Termination payments are made only upon separation from State service and only to employees hired prior to October 1, 1980. Payments at retirement or death are based on 50% of the employees' sick leave accumulation times their last rate of pay. When separating for any other reason, employees are paid a percentage of their unused sick leave that increases from 0 to 50%, depending upon the balance of their sick leave hours. Sick leave is valued at 0 to 50% plus the State's share of social security contributions, based on the pay rates in effect as of September 30, 2011.

The State instituted a banked leave time program in fiscal year 2003-04 whereby eligible employees worked a regular schedule but received pay for a reduced number of hours. The banked leave time program was continued in fiscal years 2004-05 and 2005-06. The program was discontinued in fiscal year 2005-06. The unpaid hours worked accrued to a banked leave time account. Upon an employee's separation, death, or retirement from State service, unused banked leave time hours shall be contributed by the State to the employee's account within the State's 401(k) plan and, if applicable, to the State's 457 plan. The banked leave liability, included with the annual leave liability, is valued at the pay rates in effect as of September 30, the fiscal year-end.

The estimated compensated absences liabilities for DMVA employees for the fiscal years ended September 30, 2011 and September 30, 2010 are reported in the following table:

	September 30	
	2011	2010
Annual leave	\$ 4,446,218	\$ 5,294,785
Sick leave	\$ 487,717	\$ 844,727

**Note 8 Pension Benefits**

State classified employees who work on DMVA programs are covered by two single employer pension plans offered by the State of Michigan: the State Employees' Defined Benefit Retirement Plan and the State Employees' Defined Contribution Retirement Plan (Plans). Detailed information regarding the Plans' descriptions, accounting policies, vesting and eligibility requirements, actuarial cost methods and assumptions, funding status and requirements, and 10-year historical trend information are provided in the Plans' detailed financial reports.

In addition to the Plans, State classified employees have the option to invest a portion of their salaries into 401(k) and 457 deferred compensation plans. Generally, DMVA does not make any contributions to the deferred compensation plans.

For the State Employees' Defined Benefit Retirement Plan, DMVA was billed and paid 37.4% (\$10,650,494) and 33.3% (\$10,363,457) of its payroll costs for pension charges and retiree postemployment benefits in fiscal years 2010-11 and 2009-10, respectively. For the State Employees' Defined Contribution Retirement Plan, DMVA is required to make a contribution of 4% of the annual payroll and to match employee contributions up to 3% of annual covered payroll. DMVA contributions totaled \$1,578,340 and \$1,527,537 for fiscal years 2010-11 and 2009-10, respectively. The Plans' detailed financial statements can be obtained from the Office of Retirement Services, Department of Technology, Management, and Budget, 7150 Harris Drive, P.O. Box 30171, Lansing, Michigan 48909.

Note 9 Other Postemployment Benefits

State statutes require that DMVA provide certain other postemployment benefits to many of its retired employees. Health, dental, and vision benefits as well as life insurance coverage are provided to retirees. These benefits are funded on a pay-as-you-go basis.

Note 10 Risk Management

The State has elected not to purchase commercial insurance for many of the risks of losses to which it is exposed. The State is self-insured for most general liability and property losses, portions of its employee insurance benefit and employee bonding programs, automobile liability, and workers' compensation and unemployment compensation claims. Areas of risk where some level of insurance coverage is purchased include: aircraft liability, property and loss rental insurance that may be required by bond or lease agreements, portions of the State employee insurance benefits program, certain State artifacts, builder's risk coverage, boiler and machinery coverage, and employee bonding. Settled claims have not exceeded commercial coverage in any of the past 10 fiscal years.

For unemployment claims, the Unemployment Insurance Agency bills the State for the actual amount of claims paid to former State employees. The State accrues liabilities in the governmental fund financial statements for unemployment compensation, only to the extent paid by the Unemployment Insurance Agency through September 30. During fiscal years 2010-11 and 2009-10, expenditures for payments to former DMVA employees totaled \$139,347 and \$211,821, respectively. The potential liability for future payments cannot be estimated.

DMVA also paid actual workers' compensation claims and administrative fees for DMVA employees totaling \$1,251,768 and \$1,051,185 in fiscal years 2010-11 and 2009-10, respectively.

Note 11 Capital Outlay

The capital outlay line items for the fiscal years 2010-11 and 2009-10 are included in the appropriations acts for both the Department of Technology, Management, and Budget and DMVA. After 2009, the spending authority was

part of DMVA's budget bill. The capital outlay line item represents capital expenditures relating to these capital outlay appropriations. Also, DMVA incurred additional capital expenditures that are recorded in the gross expenditures line item.

**SUPPLEMENTAL  
FINANCIAL STATEMENT AND SCHEDULE**



DEPARTMENT OF MILITARY AND VETERANS AFFAIRS  
Statement of Certain General Fund Assets and Liabilities  
As of September 30

	<u>2011</u>	<u>2010</u>
<b>ASSETS</b>		
Accounts receivable from federal agencies	\$ 21,478,586	\$ 27,251,842
Due from component units	51,212	53,035
Miscellaneous accounts receivable	44,500	38,981
Inventories	43,457	43,457
Total assets	<u>\$ 21,617,755</u>	<u>\$ 27,387,315</u>
<b>LIABILITIES</b>		
Accounts payable	\$ 6,139,712	\$ 10,079,648
Deferred revenue	87,247	80,276
Due to other funds	12,625	2,672
Other liabilities	564,900	358,442
Total liabilities	<u>\$ 6,804,484</u>	<u>\$ 10,521,038</u>

This statement is not a balance sheet and is not intended to report financial position. The statement presents certain General Fund assets and liabilities that are the responsibility of the Department of Military and Veterans Affairs. The statement does not include assets and liabilities that are accounted for centrally by the State, such as land, buildings, equipment, equity in common cash, cash in transit, and warrants outstanding.

DEPARTMENT OF MILITARY AND VETERANS AFFAIRS  
Schedule of Expenditures of Federal Awards (Note 1)  
For the Period October 1, 2009 through September 30, 2011

Federal Agency/Program	CFDA * Number	Pass-Through Identification Number	For the Fiscal Year Ended September 30, 2010			
			Directly Expended by Department	Distributed to Subrecipient	In-Kind Assistance (Note 2)	Total Expended, Distributed, and In-Kind Assistance
<b>U.S. Department of Defense</b>						
Direct Programs:						
Military Construction, National Guard	12.400		\$ 19,585,087	\$	\$	\$ 19,585,087
Total Military Construction, National Guard			\$ 19,585,087	\$ 0	\$ 0	\$ 19,585,087
National Guard Military Operations and Maintenance (O&M) Projects:						
Appendix 1 Army National Guard Real Property Operations and Maintenance	12.401		\$ 25,792,318	\$	\$ 1,549,875	\$ 27,342,193
Appendix 2 Army National Guard Environmental Resources Management	12.401		2,095,076		3,474	2,098,550
Appendix 3 Army National Guard Security Guard Activities	12.401		1,294,875			1,294,875
Appendix 4 Army National Guard Electronic Security System Operations & Maintenance	12.401		177,603		280,068	457,671
Appendix 5 Army National Guard Telecommunications	12.401		1,275,152		246,900	1,522,052
Appendix 7 Army National Guard Sustainable Range Program	12.401		1,653,746		247,103	1,900,849
Appendix 10 Army National Guard Antiterrorism Program Manager Activities	12.401		97,597			97,597
Appendix 14 Office of the Chief - Administrative Services Activities	12.401		13,395		455,000	468,395
Appendix 21 Air National Guard Facilities Operations and Maintenance Activities	12.401		2,324,892		5,842,813	8,167,705
Appendix 22 Air National Guard Environmental Program Management	12.401		169,203			169,203
Appendix 23 Air National Guard Security Guard Services	12.401		2,554,661			2,554,661
Appendix 24 Air National Guard Fire Protection Activities	12.401		3,704,352		30,075	3,734,427
Appendix 28 Air National Guard CRTC Services Program Management	12.401		228,372		223,268	451,640
Appendix 30 Air National Guard CRTC Base Operations Support	12.401		149,553			149,553
Appendix 40 Army National Guard Distance Learning Project	12.401		86,706		290,000	376,706
Total Non-ARRA National Guard Military Operations and Maintenance (O&M) Projects			\$ 41,617,501	\$ 0	\$ 9,168,576	\$ 50,786,077
Cooperative Agreement for Air National Guard CRTC Services Program Management	12.401					0
ARRA - National Guard Military Operations and Maintenance (O&M) Projects	12.401		4,587,594		2,693,661	7,281,255
Total National Guard Military Operations and Maintenance (O&M) Projects			\$ 46,205,095	\$ 0	\$ 11,862,237	\$ 58,067,332
National Guard ChalleNGe Program:						
ChalleNGe Program	12.404		\$ 2,341,603	\$	\$	\$ 2,341,603
Starbase Program	12.404			2,075,780		2,075,780
Total National Guard ChalleNGe Program			\$ 2,341,603	\$ 2,075,780	\$ 0	\$ 4,417,383
<b>Total U.S. Department of Defense</b>			<b>\$ 68,131,785</b>	<b>\$ 2,075,780</b>	<b>\$ 11,862,237</b>	<b>\$ 82,069,802</b>
<b>U.S. Department of Justice</b>						
Direct Program:						
Public Safety Partnership and Community Policing Grants	16.710		\$ 39,277	\$	\$	\$ 39,277
<b>Total U.S. Department of Justice</b>			<b>\$ 39,277</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 39,277</b>

This schedule continued on next page.

For the Fiscal Year Ended September 30, 2011				Total Expended, Distributed, and In-Kind Assistance for the Two-Year Period (Note 3)
Directly Expended by Department	Distributed to Subrecipient	In-Kind Assistance (Note 2)	Total Expended, Distributed, and In-Kind Assistance	
\$ 6,197,432	\$	\$	\$ 6,197,432	\$ 25,782,519
\$ 6,197,432	\$ 0	\$ 0	\$ 6,197,432	\$ 25,782,519
\$ 25,284,497	\$	\$ 1,975,928	\$ 27,260,425	\$ 54,602,618
1,719,765		116,704	1,836,469	3,935,019
1,163,035			1,163,035	2,457,910
133,604		211,500	345,104	802,775
1,303,320		220,100	1,523,420	3,045,472
1,383,681		41,604	1,425,285	3,326,134
98,483			98,483	196,080
4,439		218,984	223,423	691,818
2,452,365		4,013,018	6,465,383	14,633,088
117,647		148,568	266,215	435,418
2,412,566			2,412,566	4,967,227
5,025,114		132,514	5,157,628	8,892,055
75,380			75,380	451,640
99,908		361,318	461,226	224,933
\$ 41,273,804	\$ 0	\$ 7,440,238	\$ 48,714,042	\$ 99,500,119
240,935		258,255	499,190	499,190
515,858		2,754,573	3,270,431	10,551,686
\$ 42,030,597	\$ 0	\$ 10,453,066	\$ 52,483,663	\$ 110,550,995
\$ 2,508,460	\$ 2,116,151	\$	\$ 2,508,460	\$ 4,850,063
	2,116,151		2,116,151	4,191,931
\$ 2,508,460	\$ 2,116,151	\$ 0	\$ 4,624,611	\$ 9,041,994
\$ 50,736,489	\$ 2,116,151	\$ 10,453,066	\$ 63,305,706	\$ 145,375,508
\$ 181,896	\$	\$	\$ 181,896	\$ 221,173
\$ 181,896	\$ 0	\$ 0	\$ 181,896	\$ 221,173

DEPARTMENT OF MILITARY AND VETERANS AFFAIRS  
Schedule of Expenditures of Federal Awards (Note 1)  
For the Period October 1, 2009 through September 30, 2011  
Continued

Federal Agency/Program	CFDA * Number	Pass-Through Identification Number	For the Fiscal Year Ended September 30, 2010			
			Directly Expended by Department	Distributed to Subrecipient	In-Kind Assistance (Note 2)	Total Expended, Distributed, and In-Kind Assistance
<b>U.S. Department of Veterans Affairs</b>						
Direct Programs:						
ARRA - Grants to States for Construction of State Home Facilities	64.005		\$ 480,500	\$	\$	\$ 480,500
Veterans State Domiciliary Care	64.014		1,161,393			1,161,393
Veterans State Nursing Home Care	64.015		26,472,217			26,472,217
<b>Total U.S. Department of Veterans Affairs (Note 4)</b>			<b>\$ 28,114,110</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 28,114,110</b>
<b>U.S. Department of Health and Human Services</b>						
Pass-Through Program:						
Michigan Department of Community Health Public Health Emergency Preparedness	93.069	20110663	\$	\$	\$	\$
Centers For Disease Control and Prevention - Investigations and Technical Assistance	93.283	20100926	100,000			100,000
<b>Total U.S. Department of Health and Human Services</b>			<b>\$ 100,000</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 100,000</b>
Total Expenditures of Federal Awards			<b>\$ 96,385,172</b>	<b>\$ 2,075,780</b>	<b>\$ 11,862,237</b>	<b>\$ 110,323,189</b>

\* CFDA is defined as the *Catalog of Federal Domestic Assistance*.

The accompanying notes are an integral part of this schedule.

For the Fiscal Year Ended September 30, 2011				Total Expended, Distributed, and In-Kind Assistance for the Two-Year Period (Note 3)
Directly Expended by Department	Distributed to Subrecipient	In-Kind Assistance (Note 2)	Total Expended, Distributed, and In-Kind Assistance	
\$ 73,517	\$	\$	\$ 73,517	\$ 554,017
1,162,449			1,162,449	2,323,842
25,489,151			25,489,151	51,961,368
<b>\$ 26,725,117</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 26,725,117</b>	<b>\$ 54,839,227</b>
\$ 90,000	\$	\$	\$ 90,000	\$ 90,000
				100,000
<b>\$ 90,000</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 90,000</b>	<b>\$ 190,000</b>
\$ 77,733,502	\$ 2,116,151	\$ 10,453,066	\$ 90,302,719	\$ 200,625,908

## Notes to the Schedule of Expenditures of Federal Awards

### Note 1 Basis of Presentation

This schedule presents the federal grant activity of the Department of Military and Veterans Affairs (DMVA) on the modified accrual basis of accounting and in accordance with the requirements of U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the financial statements.

### Note 2 In-Kind Assistance\*

As part of the National Guard Bureau Cooperative Agreement, the U.S. Department of Defense provided in-kind assistance in the form of direct federal payment for services and supplies for the military operations and maintenance projects. The in-kind assistance dollar amounts reported on the schedule of expenditures of federal awards were determined and obtained from the Michigan U.S. Property and Fiscal Office.

### Note 3 Federal Revenue

The amounts of expenditures reported on this schedule are not comparable to the federal revenue as shown on the statement of General Fund revenues and other financing sources for DMVA. The differences are attributable to in-kind assistance and accounts payable write-offs related to Military Construction, National Guard (CFDA 12.400) and National Guard Military Operations and Maintenance (O&M) Projects (CFDA 12.401).

### Note 4 Medicare and Medicaid Revenue

The Grand Rapids Home for Veterans and the D.J. Jacobetti Home for Veterans received federal Medicare revenue totaling \$2,647,187 in fiscal year 2009-10 and \$2,524,705 in fiscal year 2010-11. The Grand Rapids Home for Veterans and the D.J. Jacobetti Home for Veterans received federal Medicaid revenue totaling \$120,246 in fiscal year 2009-10 and \$81,775 in fiscal year 2010-11. Medicare and Medicaid revenue is considered a purchase of services provided by the Homes. Therefore, a purchase of service funded by Medicare and Medicaid revenue is not included in this schedule.

\* See glossary at end of report for definition.

# INDEPENDENT AUDITOR'S REPORTS ON INTERNAL CONTROL AND COMPLIANCE



STATE OF MICHIGAN  
OFFICE OF THE AUDITOR GENERAL  
201 N. WASHINGTON SQUARE  
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THOMAS H. MCTAVISH, C.P.A.  
AUDITOR GENERAL

## Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters

Major General Gregory J. Vadnais, Director  
Department of Military and Veterans Affairs  
3411 North Martin Luther King Jr. Boulevard  
Lansing, Michigan

Dear General Vadnais:

We have audited the financial statements of the Department of Military and Veterans Affairs for the fiscal years ended September 30, 2011 and September 30, 2010, as identified in the table of contents, and have issued our report thereon dated June 11, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

### Internal Control Over Financial Reporting

Management of the Department is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Department's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Department's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined in the preceding paragraph. However, we identified certain deficiencies in internal control over financial reporting, described in the accompanying schedule of findings and questioned costs in Findings 1 through 5, that we consider to be significant deficiencies in internal control over financial reporting. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

#### Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Department's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*. However, we noted other instances of noncompliance as described in the accompanying schedule of findings and questioned costs in Findings 2 through 5.

The Department's responses to the findings identified in our audit are described in the accompanying corrective action plan. We did not audit the Department's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Governor, the Legislature, management, others within the Department, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

Sincerely,

  
Thomas H. McTavish, C.P.A.  
Auditor General  
June 11, 2012



STATE OF MICHIGAN  
OFFICE OF THE AUDITOR GENERAL  
201 N. WASHINGTON SQUARE  
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THOMAS H. MCTAVISH, C.P.A.  
AUDITOR GENERAL

Independent Auditor's Report on Compliance With  
Requirements That Could Have a Direct and Material Effect on  
Each Major Program and on Internal Control Over Compliance in  
Accordance With OMB Circular A-133

Major General Gregory J. Vadnais, Director  
Department of Military and Veterans Affairs  
3411 North Martin Luther King Jr. Boulevard  
Lansing, Michigan

Dear General Vadnais:

Compliance

We have audited the Department of Military and Veterans Affairs' compliance with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the Department's major federal programs for the two-year period ended September 30, 2011. The Department's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the Department's management. Our responsibility is to express an opinion on the Department's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to in the preceding paragraph that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Department's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the Department's compliance with those requirements.

As described in Finding 8 in the accompanying schedule of findings and questioned costs, the Department did not comply with requirements regarding eligibility; matching, level of effort, and earmarking; and procurement and suspension and debarment that are applicable to its National Guard ChalleNGe Program. Compliance with such requirements is necessary, in our opinion, for the Department to comply with the requirements applicable to that program.

In our opinion, because of the effects of the noncompliance described in the preceding paragraph, the Department of Military and Veterans Affairs did not comply, in all material respects, with the requirements referred to in the first paragraph that could have a direct and material effect on the National Guard ChalleNGe Program. Also, in our opinion, the Department of Military and Veterans Affairs complied, in all

material respects, with the compliance requirements referred to in the first paragraph that could have a direct and material effect on each of its other major federal programs for the two-year period ended September 30, 2011. The results of our auditing procedures also disclosed other instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs in Findings 6 through 8.

#### Internal Control Over Compliance

Management of the Department is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Department's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be significant deficiencies or material weaknesses and, therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider certain deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs in Finding 8 to be material weaknesses.

A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs in Findings 6 through 8 to be significant deficiencies.

The Department's responses to the findings identified in our audit are described in the accompanying corrective action plan. We did not audit the Department's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Governor, the Legislature, management, others within the Department, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

Sincerely,



Thomas H. McTavish, C.P.A.

Auditor General

June 11, 2012

# SCHEDULE OF FINDINGS AND QUESTIONED COSTS

## Section I: Summary of Auditor's Results

### Financial Statements

Type of auditor's report issued: Unqualified\*

Internal control\* over financial reporting:

Material weaknesses\* identified? No

Significant deficiencies\* identified? Yes

Noncompliance or other matters material to the financial statements? No

### Federal Awards

Internal control over major programs:

Material weaknesses\* identified? Yes

Significant deficiencies\* identified? Yes

Type of auditor's report issued on compliance for major programs:

Unqualified for all major programs except for the National Guard ChalleNGe Program, which is adverse\*.

Any audit findings disclosed that are required to be reported in accordance with U.S. Office of Management and Budget\* (OMB) Circular A-133, Section 510(a)? Yes

Identification of major programs:

<u>CFDA* Number</u>	<u>Name of Federal Program</u>
12.400	Military Construction, National Guard
12.401	<u>National Guard Military Operations and Maintenance (O&amp;M) Projects:</u> <ul style="list-style-type: none"> <li>• National Guard Military Operations and Maintenance (O&amp;M) Projects</li> <li>• ARRA - National Guard Military Operations and Maintenance (O&amp;M) Projects</li> </ul>

\* See glossary at end of report for definition.

12.404	National Guard Challenge Program
64.015	Veterans State Nursing Home Care

Dollar threshold used to distinguish between type A and type B programs: \$3,000,000

Auditee qualified as a low-risk auditee\*? No

## Section II: Findings Related to the Financial Statements

### **FINDING (5111201)**

#### 1. Schedule of Expenditures of Federal Awards (SEFA)

The Department of Military and Veterans Affairs' (DMVA's) internal control over financial reporting did not ensure that DMVA prepared its SEFA in accordance with OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

OMB Circular A-133 requires DMVA to prepare appropriate financial statements, including the SEFA, and to maintain internal control that provides reasonable assurance regarding the reliability of its financial reporting. Internal control is a process, effected by those charged with governance, management, and other personnel, designed to provide reasonable assurance about the achievement of the entity's objectives with regard to the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations. Further, Section 18.1485 of the *Michigan Compiled Laws* requires DMVA to establish and maintain an internal accounting and administrative control system that includes recordkeeping procedures to control assets, liabilities, revenues, and expenditures.

DMVA's processes and procedures for preparing its SEFA did not ensure a complete and accurate reporting of federal awards expended on its SEFA. Our

\* See glossary at end of report for definition.

review of DMVA's internal control over financial reporting for the SEFA preparation process and DMVA's SEFA disclosed:

- a. DMVA did not include all expenditures of federal awards on its SEFA. As a result, DMVA understated the amounts expended on the SEFA by \$39,277.

Section 310(b)(1) of OMB Circular A-133 requires that the SEFA include each individual federal program and provide total federal awards expended for each individual federal program.

We determined that DMVA did not include the federal expenditures for the U.S. Department of Justice's Public Safety Partnership and Community Policing Grants (*CFDA* 16.710) on its fiscal year 2009-10 SEFA. Federal expenditures for *CFDA* 16.710 totaled \$39,277 for fiscal year 2009-10.

- b. DMVA did not accurately classify the total amounts directly expended and the total amount distributed to its subrecipient\*. As a result, DMVA overstated expenditures directly expended and understated expenditures distributed to its subrecipient by \$2,116,151 for the National Guard ChalleNGe Program (*CFDA* 12.404) on its fiscal year 2010-11 SEFA.

Section 310(b)(5) of OMB Circular A-133 requires pass-through entities\* to identify in the SEFA the total amount provided to subrecipients from each federal program.

- c. DMVA incorrectly reported expenditures for National Guard Military Operations and Maintenance (O&M) Projects (*CFDA* 12.401) on its SEFA for fiscal year 2010-11. As a result, DMVA overstated O&M Projects Program Appendix 28 expenditures and understated expenditures for the Cooperative Agreement for Air National Guard CRTC Services Program Management by \$240,935 on its fiscal year 2010-11 SEFA.

DMVA administers the O&M Projects Program under cooperative agreements with the U.S. Department of Defense. The specific activities to be carried out under the cooperative agreements are enumerated in appendixes and

\* See glossary at end of report for definition.

presented separately on DMVA's SEFA. We determined that DMVA did not assign new account coding in the accounting records when a new Cooperative Agreement for Air National Guard CRTC Services Program Management was entered into to replace the existing Appendix 28 Program, which ended. Instead, DMVA recorded accounting entries related to the new Cooperative Agreement for Air National Guard CRTC Services Program Management to the same account coding that had been previously established for Appendix 28. As a result, DMVA incorrectly presented expenditures for the Cooperative Agreement for Air National Guard CRTC Services Program Management as Appendix 28 expenditures on its SEFA.

- d. DMVA's accounting records did not support the expenditures as presented on the SEFA. As a result, DMVA overstated total federal expenditures by \$260,985 on its SEFA for fiscal year 2010-11. We noted:
  - (1) DMVA identified total federal expenditures of \$260,985 for fiscal year 2010-11 for ARRA - Grants to States for Construction of State Home Facilities (*CFDA* 64.005). However, DMVA did not receive a grant award during the audit period for Grants to States for Construction of State Home Facilities. As a result, the SEFA was overstated by \$260,985 for fiscal year 2010-11 for ARRA - Grants to States for Construction of State Home Facilities (*CFDA* 64.005).
  - (2) DMVA did not record required adjusting entries in the accounting records to ensure proper presentation of the appendix expenditures for National Guard Military Operations and Maintenance (O&M) Projects (*CFDA* 12.401). DMVA prepared manual adjustments totaling \$1,078,100 to properly move expenditures between appendixes. As a result, the accounting records did not support the amounts reported on the SEFA. We determined that the amounts presented for the appendix expenditures on the SEFA were proper. However, creating manual adjustments outside of DMVA's accounting records increases the risk of incomplete or inaccurate SEFA reporting.

The errors that we noted in parts a., b., c., and d.(1) were corrected when brought to DMVA's attention and DMVA appropriately revised its SEFA presented in this report.

We reported similar conditions in our prior single audit\*. DMVA stated in its corrective action plan in the prior single audit that it would work with the U.S. Property and Fiscal Office (USPFO) and federal program managers to establish joint procedures that ensure the SEFA is prepared in accordance with OMB Circular A-133 requirements.

## **RECOMMENDATION**

We again recommend that DMVA improve its internal control over financial reporting to ensure that DMVA prepares its SEFA in accordance with OMB Circular A-133.

## **FINDING (5111202)**

### **2. Capital Asset Reporting**

DMVA's internal control was not sufficient to ensure the accuracy of its financial reporting of capital assets. As a result, certain buildings, building improvements, and land remained on the State's records as capital assets even though the State no longer owned the assets and other State-owned buildings, building improvements, and land were not reported as capital assets.

The State of Michigan Financial Management Guide (Part II, Chapter 21, Section 220) requires DMVA to report acquisitions, disposals, and renovations of capital assets to the Office of Financial Management (OFM), Department of Technology, Management, and Budget. Capital assets include land, improvements to land, buildings, building improvements, and equipment that are used in operations and that have useful lives extending beyond a single reporting period. OFM maintains records of all capital assets of the State and uses the records to prepare the State's government-wide financial statements. DMVA presents its departmental capital asset information in Note 6 to the DMVA financial statements.

Our review of DMVA capital asset reporting disclosed:

- a. DMVA did not report all capital asset disposals to OFM during our audit period. DMVA sold one armory in fiscal year 2009-10 and another armory in fiscal year 2010-11; however, DMVA did not report these disposals to OFM. As a

\* See glossary at end of report for definition.

result, the land, buildings, and building improvements for these two properties remained on the State's records as capital assets even though the State no longer owned these assets. We determined that the capital asset ending balances were overstated by the following amounts:

	Overstatements as of September 30	
	2011	2010
Land	\$ 104,163	\$ 58,788
Buildings	1,545,202	138,782
Total	<u>\$1,649,365</u>	<u>\$197,570</u>

When brought to DMVA's attention, DMVA corrected Note 6 to the financial statements.

- b. DMVA did not report all its capital assets to OFM. DMVA owns six armory buildings built in the 1910s, 1920s, and 1950s and one parcel of armory land that were not properly reported to OFM and not properly recorded in the State's capital asset records. As a result, the capital asset balances in Note 6 to the DMVA financial statements are understated by an indeterminable amount.

**RECOMMENDATION**

We recommend that DMVA improve its internal control to ensure the accuracy of its financial reporting of capital assets.

**FINDING (5111203)**

3. Revenue Classification

DMVA's internal control was not sufficient to ensure that certain revenues were properly classified by revenue source. As a result, federal revenues were overstated and revenues from services were understated by \$291,361 and \$320,587 for fiscal years 2010-11 and 2009-10, respectively. Without sufficient internal control, the risk exists that other similar errors will not be prevented, identified, or corrected.

Section 1800.115 of the *Codification of Governmental Accounting and Financial Reporting Standards*, published by the Governmental Accounting Standards Board\* (GASB), requires governmental fund revenues to be classified by fund and source.

Although errors were corrected when brought to DMVA's attention for the financial statements presented in this report, our review of DMVA's draft financial statements disclosed that DMVA had improperly classified Grand Rapids Home for Veterans (GRHV) and D.J. Jacobetti Home for Veterans (DJJHV) private medical insurance revenues as revenues from federal agencies. DMVA recorded GRHV and DJJHV private medical insurance revenues as Medicare revenues in its accounting system, resulting in the revenues being classified as federal revenues on the financial statements. Based on DMVA records, we estimate that GRHV and DJJHV should have classified \$291,361 and \$320,587 for fiscal years 2010-11 and 2009-10, respectively, as revenues from services.

We noted revenue classification errors in our prior single audit. DMVA corrected the revenue objects related to those specific errors identified in the prior single audit.

### **RECOMMENDATION**

We again recommend that DMVA improve its internal control to ensure that revenues are properly classified by revenue source.

### **FINDING (5111204)**

#### 4. Cash Management

DMVA needs to improve its internal control over its compliance with State and federal cash management requirements. As a result, DMVA has not requested federal reimbursement on a timely basis for three federal programs, resulting in lost interest to the State of an estimated \$37,138.

The DTMB Administrative Guide and Title 31, Part 205, section 33(a) of the *Code of Federal Regulations*\* (CFR) require DMVA to request and obtain funds from the

\* See glossary at end of report for definition.

federal government as close as administratively feasible to the State's actual cash outlays for federal programs.

Our review of DMVA's cash management practices disclosed:

- a. DMVA has not requested federal funds in a timely manner for expenditures incurred for two major federal programs reviewed, resulting in lost interest to the State of an estimated \$26,435:
  - (1) In the O&M Projects Program, DMVA has not submitted reimbursement requests for 22 expenditures totaling \$2.1 million that were incurred by the State in fiscal years 2008-09 and 2009-10. As a result, these expenditures remained unreimbursed for 1.7 years to 2.4 years and the State has lost interest earnings totaling an estimated \$25,885 as of September 30, 2011.
  - (2) In the Military Construction, National Guard Program, DMVA has not submitted reimbursement requests for 4 expenditures totaling \$68,000 that were incurred by the State in fiscal years 2007-08, 2008-09, and 2009-10. As a result, these expenditures remained unreimbursed for 1.2 years to 3.0 years and the State has lost interest earnings totaling an estimated \$550 as of September 30, 2011.
- b. DMVA did not request and obtain federal funds on a timely basis for two major federal programs reviewed, resulting in lost interest to the State of an estimated \$10,703:
  - (1) In the O&M Projects Program, we noted 82 expenditures for which DMVA averaged 398 days from the date of the expenditure incurrence until receiving federal reimbursement. The time for DMVA to receive federal reimbursement for these 82 expenditures ranged from 49 days to 3.5 years. As a result, the State lost interest earnings totaling an estimated \$10,703.
  - (2) In the National Guard ChalleNGe Program, for 9 (17%) of 52 expenditures, DMVA averaged 61 days from the date of the

expenditure incurrence until receiving federal reimbursement. The time for DMVA to receive federal reimbursement for these 9 expenditures ranged from 47 days to 90 days.

Cash managers need to adhere to appropriate and detailed procedures and controls, including management oversight. Effective cash management efforts should include consideration of the timing of program expenditure payments relative to federal revenue requests for reimbursement.

We noted the same condition in our two prior single audits. DMVA stated in its corrective action plan in the prior single audit that it would take corrective action by December 30, 2010 and that it would engage the USPFO as well as its federal program managers in discussions about how DMVA can further minimize the time elapsing between the transfer of federal funds and the disbursement of funds by the State.

### **RECOMMENDATION**

We again recommend that DMVA improve its internal control over its compliance with State and federal cash management requirements.

### **FINDING (5111205)**

#### **5. Procurement**

DMVA's internal control did not ensure that it complied with State procurement policies when purchasing certain services. This finding is included in Section III of the schedule of findings and questioned costs (Findings 5111207 and 5111208).

**The status of the findings related to the financial statements that were reported in prior single audits is disclosed in the summary schedule of prior audit findings.**

### **Section III: Findings and Questioned Costs\* Related to Federal Awards**

OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, requires the auditor to test key controls at a level that would provide sufficient evidence that the established control structure would provide a high probability that material federal program noncompliance would be prevented or detected and corrected. This requires that the auditor set the tolerable exception rate of occurrence at a very low level. During the audit fieldwork, the auditor, in close consultation with the auditee, identifies the key controls that the auditee has established to ensure federal program compliance. In those cases in which the auditor's tests of key controls identify exception rates in excess of the tolerable exception rate of occurrence, the auditor must generally report the observed exception rate in the report finding.

Further, Circular A-133 requires the auditor to report in this section of the audit report known questioned costs that are greater than \$10,000 for a type of compliance requirement for a major program and known questioned costs that are less than \$10,000 for a type of compliance requirement for a major program if it is likely that total questioned costs would exceed \$10,000.

As a result of these low required reporting thresholds, the reader may note that, in some cases, the observed exception rates of occurrence and reported known questioned costs appear insignificant in relation to the overall federal expenditures of the auditee. After the audit report is filed with the federal audit clearinghouse, the responsible federal agency is required to issue a management decision within six months of the receipt of the audit report. The management decision may include a request for the return of the known questioned costs.

\* See glossary at end of report for definition.

## **FINDING (5111206)**

### 6. Military Construction, National Guard, CFDA 12.400

U.S. Department of Defense	CFDA 12.400: Military Construction, National Guard
MCCA Number:	MCCA Date:
W912JB-04-2-2002	September 22, 2004
W912JB-08-2-2001	December 19, 2007
W912JB-08-2-2002	December 19, 2007
W912JB-08-2-2004	March 21, 2008
W912JB-09-2-2001	March 5, 2009
W912JB-09-2-2002	March 5, 2009
W912JB-09-2-2003	March 6, 2009
W912JB-10-2-2001	January 6, 2010
W912JB-10-2-2002	April 19, 2010
	Known Questioned Costs: \$529,844

DMVA's internal control over the Military Construction, National Guard Program did not ensure its compliance with federal laws and regulations and cooperative agreement requirements regarding period of availability of federal funds. As a result, we identified known questioned costs of \$529,844.

Internal control that does not ensure compliance with federal laws and regulations could result in sanctions, disallowances, and/or future reductions of Military Construction, National Guard Program awards.

Federal expenditures for the Military Construction, National Guard Program totaled \$25.8 million for the two-year period ended September 30, 2011.

During fiscal years 2003-04, 2007-08, 2008-09, and 2009-10, the federal National Guard Bureau (NGB) and the State of Michigan entered into 9 Military Construction Cooperative Agreements (MCCAs) for various construction projects. DMVA completed 5 of these projects before or during our audit period. For those projects completed before our audit period, DMVA made payments to contractors and requested Military Construction, National Guard Program reimbursement during our audit period.

DMVA and the National Guard USPFO complete an NGB project inspection report (form 593R) at half and final completion of each Military Construction project. National Guard Regulation 5-1 and Section 306 of the MCCA stipulate that within 90 days of final completion of a Military Construction project or upon termination of the MCCA, whichever comes earlier, DMVA shall promptly deliver to the NGB a full and final accounting liquidating all payments or reimbursements under the MCCA. Section 306 of the MCCA also states that the 90-day time frame begins when NGB form 593R is completed by the State and the USPFO. Costs incurred for performance of the project which are not disclosed by DMVA within 90 days of the final completion of the project shall not be eligible for reimbursement by the NGB. At its sole discretion, the NGB may extend the 90-day limit for good cause shown.

DMVA did not deliver to the NGB full and final accountings liquidating all payments or reimbursements within 90 days of the final completion for all 5 projects reviewed or obtain the NGB's approval to extend the 90-day limit. Our procedures identified 6 reimbursements for which DMVA's request was after the 90-day limit, and 2 of the 6 reimbursements were 90 days or more past the 90-day limit. We determined that DMVA had not implemented internal control to ensure the timely delivery to the NGB of full and final accountings liquidating all payments or reimbursements for completed projects. As a result, we questioned costs totaling \$529,844.

We reported the same condition in our two prior single audits. DMVA stated in its corrective action plan in the prior single audit that it would work with federal program managers and the USPFO to develop joint operating procedures to ensure that NGB form 593-R is properly completed and signed in a timely manner.

## **RECOMMENDATION**

We again recommend that DMVA strengthen its internal control over the Military Construction, National Guard Program to ensure its compliance with federal laws and regulations and cooperative agreement requirements regarding period of availability of federal funds.

**FINDING (5111207)**

7. National Guard Military Operations and Maintenance (O&M) Projects and ARRA - National Guard Military Operations and Maintenance (O&M) Projects, CFDA 12.401

U.S. Department of Defense	CFDA 12.401: National Guard Military Operations and Maintenance (O&M) Projects CFDA 12.401: ARRA - National Guard Military Operations and Maintenance (O&M) Projects
<p>Special Military Cooperative Agreement: W912JB-09-2-9005</p> <p>Master Cooperative Agreement: W912JB-10-2-1000</p> <p>Special Military Project Cooperative Agreement: W912JB-11-2-3076</p>	<p>Award Period: 07/07/2009 - 09/30/2012</p> <p>Appendix 1 Army National Guard Real Property Operations and Maintenance</p> <p>Appendix 2 Army National Guard Environmental Resources Management</p> <p>Appendix 3 Army National Guard Security Guard Activities</p> <p>Appendix 4 Army National Guard Electronic Security System Operations &amp; Maintenance</p> <p>Appendix 5 Army National Guard Telecommunications</p> <p>Appendix 7 Army National Guard Sustainable Range Program</p> <p>Appendix 10 Army National Guard Antiterrorism Program Manager Activities</p> <p>Appendix 14 Office of the Chief - Administrative Services Activities</p> <p>Appendix 21 Air National Guard Facilities Operations and Maintenance Activities</p> <p>Appendix 22 Air National Guard Environmental Program Management</p> <p>Appendix 23 Air National Guard Security Guard Services</p> <p>Appendix 24 Air National Guard Fire Protection Activities</p> <p>Appendix 28 Air National Guard CRTC Services Program Management</p> <p>Appendix 30 Air National Guard CRTC Base Operations Support</p> <p>Appendix 40 Army National Guard Distance Learning Project</p> <p>Cooperative Agreement for Air National Guard CRTC Services Program Management</p>
	Known Questioned Costs: \$2,293,436

DMVA's internal control over the O&M Projects Program did not ensure compliance with federal laws and regulations regarding activities allowed or unallowed and allowable costs/cost principles. Also, DMVA's internal control did not ensure compliance with the American Recovery and Reinvestment Act of 2009\* (ARRA) requirements regarding the Davis-Bacon Act and procurement and suspension and debarment for O&M Projects funded by ARRA. As a result, we identified known questioned costs of \$2,293,436.

Internal control that does not ensure compliance with federal laws and regulations could result in sanctions, disallowances, and/or future reductions of O&M Projects Program awards.

Federal expenditures for the O&M Projects Program totaled \$110.6 million for the two-year period ended September 30, 2011, of which \$10.6 million were ARRA expenditures.

Our exceptions, by compliance area, are as follows:

a. Activities Allowed or Unallowed

DMVA charged expenditures to and obtained reimbursement from Appendix 28 in fiscal year 2009-10 without establishing a signed appendix with the NGB. Because DMVA did not have a signed Appendix 28 prior to incurring expenditures and obtaining reimbursement, we identified known questioned costs totaling \$228,372.

The NGB and DMVA entered into a Master Cooperative Agreement (MCA) for federal reimbursement of operations and maintenance costs for the State's military facilities. The scope of the MCA included all activities enumerated in the appendixes. Without an approved appendix in place, the costs incurred were not for allowed activities.

We reported the same condition in our prior single audit. DMVA stated in its corrective action plan in the prior single audit that DMVA was working with the USPFO Grants Officer Representative to establish joint procedures for the initial funding, amendment, and closeout modification processes.

\* See glossary at end of report for definition.

b. Allowable Costs/Cost Principles

Our review of allowable costs/cost principles disclosed:

- (1) DMVA did not maintain approved time sheets throughout the audit period for 4 (57%) of 7 federally funded employees in one timekeeping unit. Without approved time sheets, DMVA cannot provide certification that 100% of the employees' activities were related to the federal program. As a result, we identified known questioned costs totaling \$429,902.

Appendix B of OMB Circular A-87 (federal regulation 2 *CFR* 225) requires that employees who are expected to work solely on a single federal program must provide periodic certifications that they have worked solely on that program for the period covered by the certification. DMVA's policy is to document this certification via biweekly signatures of the employee and supervisor on the employee's time sheet. The employee's and supervisor's signatures certify that 100% of the employee's activities were related to the federal program.

- (2) DMVA did not ensure that payroll costs were charged to the appropriate federal programs.

Appendix A of OMB Circular A-87 (federal regulation 2 *CFR* 225) states that costs must be necessary and reasonable for the performance and administration of federal awards. Also, National Guard Regulation 5-1, section 5-6 states that the State Military Department shall take particular care to ensure that it does not charge costs incurred in performance of one cooperative agreement to another, or to both.

Our review disclosed that DMVA improperly charged 100% of one employee's payroll costs to O&M Projects Program awards. The employee's duties included activities that were not directly chargeable to the O&M Projects Program. We determined that 60% of the employee's time was related to the O&M Projects Program. As a result, we identified known questioned costs totaling \$76,971.

We reported the same condition in our prior single audit. DMVA stated in its corrective action plan in the prior single audit that DMVA would implement a process to certify this federally funded employee on duties associated with the position.

c. Davis-Bacon Act

DMVA's internal control did not ensure that construction contracts properly contained Davis-Bacon Act clauses.

Section 1606 of ARRA and the OMB implementing guidance for ARRA require that all laborers and mechanics employed by contractors or subcontractors to work on construction contracts in excess of \$2,000 financed by federal assistance funds must be paid wages not less than those established for the locality for the project by the U.S. Department of Labor.

DMVA did not include Davis-Bacon Act clauses and certifications within one contract to inform the contractor of the requirement to pay prevailing federal wage rates. Although DMVA did not include Davis-Bacon Act clauses and certifications within the contract, the contractor did provide DMVA with weekly payroll reports to support that appropriate wages were paid.

We reported the same condition in our prior single audit. DMVA stated in its corrective action plan in the prior single audit that it would establish internal control procedures to monitor compliance with ARRA requirements.

d. Procurement and Suspension and Debarment

DMVA's internal control did not ensure that construction contracts properly contained "Buy American" requirements. As a result, we identified known questioned costs of \$1,558,191.

Section 1605 of ARRA and the OMB implementing guidance for ARRA prohibit the use of ARRA funds for a project for construction, alteration, maintenance, or repair of a public building or public work unless all of the iron, steel, and manufactured goods used in the project are produced in the United States.

DMVA did not include Buy American award terms or clauses within three contracts to ensure that its contractors followed ARRA Buy American requirements. As a result, DMVA did not require or obtain certifications and evidence from the three contractors that materials used for the ARRA-funded projects complied with the Buy American requirements.

We reported the same condition in our prior single audit. DMVA stated in its corrective action plan in the prior single audit that it would establish internal control procedures to monitor compliance with ARRA requirements.

**RECOMMENDATIONS**

We again recommend that DMVA strengthen its internal control over the O&M Projects Program to ensure compliance with federal laws and regulations regarding activities allowed or unallowed and allowable costs/cost principles.

We also again recommend that DMVA improve its internal control over O&M Projects funded by ARRA to ensure compliance with ARRA requirements regarding the Davis-Bacon Act and procurement and suspension and debarment.

**FINDING (5111208)**

8. National Guard ChalleNGe Program, CFDA 12.404

U.S. Department of Defense	CFDA 12.404: National Guard ChalleNGe Program
Award Number: ChalleNGe:	Award Period:
W912JB-09-2-4001	01/01/2009 - 12/31/2009
W912JB-09-2-4001	01/01/2010 - 12/31/2010
W912JB-09-2-4001	01/01/2011 - 12/31/2011
W912JB-09-2-4003	10/01/2009 - 09/30/2010
W912JB-09-2-4003	10/01/2010 - 09/30/2011
Starbase:	
W912JB-09-2-4002	10/01/2009 - 09/30/2010
W912JB-09-2-4002	10/01/2010 - 09/30/2011
	Known Questioned Costs: \$4,823,928

DMVA did not comply with National Guard ChalleNGe (NGC) Program federal laws and regulations and cooperative agreements concerning eligibility. Also, DMVA's

internal control over the NGC Program did not ensure its compliance with federal laws and regulations and cooperative agreements regarding eligibility; matching, level of effort and earmarking; procurement and suspension and debarment; and reporting. Our review disclosed material weaknesses in internal control and material noncompliance\* with federal laws and regulations and cooperative agreements regarding eligibility; matching, level of effort, and earmarking; and procurement and suspension and debarment. As a result, we issued an adverse opinion on compliance with federal laws and regulations and cooperative agreements for the NGC Program. We also identified known questioned costs of \$4,823,928.

Noncompliance with federal program requirements could result in sanctions, disallowances, and/or future reductions in NGC Program awards.

The NGC Program in Michigan comprises two separate subprograms: ChalleNGe and Starbase. Federal expenditures for the NGC Program totaled \$9.0 million for the two-year period ended September 30, 2011, of which DMVA expended \$4.9 million for the ChalleNGe Program and distributed \$4.2 million to the Starbase Academy as a subrecipient.

Our exceptions, by compliance area, are as follows:

a. Eligibility

DMVA did not comply with federal laws and regulations and cooperative agreements concerning cadet eligibility related to school enrollment and employment status for the ChalleNGe Program. Also, DMVA's internal control did not ensure compliance with federal laws and regulations and cooperative agreements concerning cadet eligibility related to drug testing requirements for the ChalleNGe Program.

Our review of ChalleNGe Program eligibility disclosed:

- (1) DMVA did not maintain documentation of secondary school dropout status for 38 (95%) of 40 cadets sampled. Based on interview notes within the cadet files, 22 (58%) of the 38 cadets stated that they were still

\* See glossary at end of report for definition.

enrolled at a secondary school at the time they applied for enrollment in the ChalleNGe Program. DMVA informed us that when applicants are interviewed, ChalleNGe Program staff encourage applicants who are still enrolled in secondary school to stay in school because they are less likely to make decisions, such as using drugs and committing crimes, that would prevent their acceptance into the ChalleNGe Program. However, this practice conflicts with ChalleNGe Program eligibility requirements.

Section 4.10.2 of the Master Youth Programs Cooperative Agreement (MYPCA) states that the selection of participants for the program shall be from applicants who are a school dropout from secondary school. Also, Title 32, section 509(e) of the *United States Code* states that "A school dropout from secondary school shall be eligible to participate in the [National Guard ChalleNGe] Program." Section E2.1.19 of Department of Defense Instruction 1025.8 defines a school dropout as a youth who is no longer attending any school and who has not received a secondary school diploma or certificate from a program of equivalency for such diploma. The preceding requirements do not indicate that participants are eligible if they drop out of secondary school to attend the ChalleNGe Program.

We reported the same condition in our prior single audit. DMVA stated in its corrective action plan in the prior single audit that the dropout timing is a national issue and cannot be resolved by the states, but at the federal level by the NGC Program.

- (2) DMVA did not verify that ChalleNGe Program applicants were unemployed or underemployed for the 40 (100%) cadets sampled. ChalleNGe Program management informed us that documentation does not exist to determine if the cadets were unemployed or underemployed. Rather, ChalleNGe Program management informed us that it believes that program participation and the willingness to volunteer show the need to obtain the skills and education necessary to be a productive member of society.

Section 4.10.4 of the MYPCA states that the selection of participants for the program shall be from applicants who are unemployed or underemployed.

- (3) DMVA did not maintain documentation of drug test results for two entire cadet classes and for the female cadets of another cadet class for the 5 cadet classes that ended or began during the audit period. Based on the number of cadets who were accepted into the pre-ChalleNGe phase, drug test results were not available for 336 (50%) of 678 cadets. ChalleNGe Program management stated that every cadet is drug tested on the first day of pre-ChalleNGe to ensure that he or she meets this eligibility requirement. However, without drug test results, we could not determine that the cadets who were accepted into the ChalleNGe Program were free from the use of illegal drugs.

Section 4.10.6 of the MYPCA states that the selection of participants for the program shall be from applicants who are free from the use of illegal drugs or substances.

We could not determine the ChalleNGe Program costs directly associated with the ineligible cadets as DMVA is not reimbursed on a per pupil basis.

b. Matching, Level of Effort, and Earmarking

DMVA's internal control did not ensure compliance with federal laws and regulations and cooperative agreements concerning matching, level of effort, and earmarking requirements for the ChalleNGe Program. As a result, we identified known questioned costs totaling \$631,997.

Our review of matching, level of effort, and earmarking disclosed:

- (1) DMVA did not meet the 40% State match requirement for the ChalleNGe Program 2009 budget year (January 1, 2009 through December 31, 2009). DMVA's 2009 budget year final accounting report showed that DMVA matched only 38.9% of program expenditures for the budget year ended December 31, 2009. Total federal expenditures for the 2009

budget year totaled \$2,458,725, of which \$638,199 were related to the current audit period. As a result, we reported known questioned costs totaling \$104,690.

- (2) DMVA did not meet the 25% State match requirement for the ChalleNGe Program 2010 budget year (January 1, 2010 through December 31, 2010). DMVA improperly included Title I funds toward its 2010 budget year State match totals. As a result, the State did not meet its match requirements for the 2010 budget year resulting in known questioned costs totaling \$527,307.

Federal regulation 32 *CFR* 33.24 states that DMVA cannot include costs borne by another federal grant toward its match requirement. The Title I funds used toward DMVA's match were ultimately funded under the U.S. Department of Education's Title I grant and, as a result, were not eligible to be counted toward DMVA's State match requirement.

Attachment A to Appendix 1 of the MYPKA states that the amount of assistance provided to a state for the ChalleNGe Program may not exceed 60% of the costs of operating the state program during the year. As a result, the State is responsible for 40% of the program cost in the 2009 budget year. For the 2010 budget year, Title 32, section 509(d)(1) of the *United States Code* was amended by decreasing the State's share of program costs to 25%.

c. Procurement and Suspension and Debarment

DMVA's internal control did not ensure compliance with federal laws and regulations regarding procurement and suspension and debarment. As a result, we identified known questioned costs totaling \$4,191,931. Our review of procurement and suspension and debarment disclosed:

- (1) DMVA did not follow State procurement policies when procuring services for the Starbase Academy. DMVA entered into a grant agreement with its subrecipient to run the Starbase Academy; however, DMVA did not obtain State Administrative Board approval and did not competitively bid the procurement. As a result, we identified known questioned costs totaling \$4,191,931.

In addition, DMVA did not execute this grant agreement in a timely manner. The grant agreement was effective beginning October 1, 2009; however, DMVA did not execute the agreement until late December 2010, nearly 15 months after the effective date of the agreement. DMVA expended \$2,310,102 during this nearly 15-month period that an executed agreement was not in place.

Federal regulation 32 *CFR* 33 requires DMVA to follow the same policies and procedures that it uses for procurements from its nonfederal funds. Also, Article IX, Section 901 of the MYPCA states that the acquisition of goods and services shall be according to applicable State contracting procedures. State procurement policy requires that contracts in excess of \$250,000 be approved by the State Administrative Board and be competitively bid.

- (2) DMVA had not documented that contractors were not on the federal Excluded Parties List System for the 3 contracts sampled. Thus, we could not verify that DMVA's internal control provided assurance that contractors were not suspended or debarred prior to DMVA entering into the related contract.

Section 808 of the MYPCA states that recipients shall not make any award or permit any award (subgrant or contract) at any tier to any party that is debarred or suspended or is otherwise excluded from or ineligible for participation in federal assistance programs under Executive Order No. 12549.

We reviewed the federal Excluded Parties List System and verified that none of the contractors in our sample of NGC Program expenditures were actually suspended or debarred during the respective fiscal years. As a result, we did not report any questioned costs for this item. However, without a formal process to verify the status of contractors, a risk exists that other, or future, contractors could be suspended or debarred.

d. Reporting

DMVA's internal control did not ensure compliance with the reporting requirements of the NGC Program.

Our review disclosed that DMVA submitted 14 (31%) of the 45 sampled monthly reimbursement requests late during our audit period. DMVA submitted the reimbursement requests 1 day to 42 days late, averaging 11.3 days late.

The MYPCA requires DMVA to request periodic reimbursement by submitting a certified statement, no less than once a month, itemizing the amount of funds expended during the preceding month.

We reported the same condition in our prior two single audits. DMVA stated in its corrective action plan in the prior single audit that it would establish a formal procedure for its monthly review of requests for reimbursement.

## **RECOMMENDATIONS**

We again recommend that DMVA comply with NGC Program federal laws and regulations and cooperative agreements concerning eligibility.

We also again recommend that DMVA implement effective internal control to ensure its compliance with federal laws and regulations and cooperative agreements regarding reporting.

We further recommend that DMVA strengthen internal control to ensure its compliance with federal laws and regulations and cooperative agreements regarding eligibility; matching, level of effort, and earmarking; and procurement and suspension and debarment.

**The status of the findings related to federal awards that were reported in prior single audits is disclosed in the summary schedule of prior audit findings.**

## OTHER SCHEDULES

DEPARTMENT OF MILITARY AND VETERANS AFFAIRS

Summary Schedule of Prior Audit Findings

As of June 11, 2012

**PRIOR AUDIT FINDINGS RELATED TO THE FINANCIAL STATEMENTS**

Audit Findings That Have Been Fully Corrected:

**Audit Period:** October 1, 2005 through September 30, 2007  
**Finding Number:** 5110801F  
**Finding Title:** Schedule of Expenditures of Federal Awards (SEFA)

**Finding:** The Department of Military and Veterans Affairs' (DMVA's) internal control over financial reporting did not ensure that it prepared its SEFA in accordance with U.S. Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and State financial management policies.

**Agency Comments:** Corrective action complete. DMVA has taken steps to ensure that all federal awards are properly identified and accounted for on the SEFA and has established procedures to ensure that DMVA prepares its SEFA in accordance with OMB Circular A-133 and State financial management policies. DMVA prepared the fiscal year 2005-06 and 2006-07 SEFAs on the modified accrual basis of accounting.

**Audit Period:** October 1, 2005 through September 30, 2007  
**Finding Number:** 5110803F  
**Finding Title:** Internal Control Over Accounting Transaction Processing

**Finding:** DMVA did not always separate the initiation and release of accounting transaction functions and did not have compensating controls for the lack of separation of duties.

**Agency Comments:** Corrective action complete. DMVA has reaffirmed with staff the importance of separation of duties and how segregation of these two functions help guard against unintentional errors. Additional staff have been assigned in an effort to eliminate instances of the same individual initiating and releasing accounting transactions. DMVA will initiate periodic reviews through the use of data queries and other methods to ensure compliance. If an emergency situation arises where an individual employee must enter and release a payment document, the reason must be noted on the payment document.

**Audit Period:** October 1, 2005 through September 30, 2007

**Finding Number:** 5110804F

**Finding Title:** Internal Control Over Food Purchases and Receipt

**Finding:** DMVA did not have sufficient internal control over the purchase and receipt of food items at its Grand Rapids Home for Veterans (GRHV).

**Agency Comments:** Corrective action complete. DMVA has strengthened its internal control process to ensure that all necessary documentation relative to the purchase, receipt, and authorization of food items is in place.

**Audit Period:** October 1, 2005 through September 30, 2007

**Finding Number:** 5110805F

**Finding Title:** Internal Control Over Records Retention

**Finding:** DMVA did not have internal control to ensure that it maintained and safeguarded its hard copy accounting records.

**Agency Comments:** Corrective action complete. DMVA has developed and implemented an internal control policy and procedure to ensure that the hard copies of accounting records are stored and

destroyed in compliance with State of Michigan records retention schedules.

**Audit Period:** October 1, 2007 through September 30, 2009  
**Finding Number:** 5111001  
**Finding Title:** Schedule of Expenditures of Federal Awards (SEFA)

**Finding:** DMVA's internal control over financial reporting did not ensure that it prepared its SEFA in accordance with OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

**Agency Comments:** Corrective action complete. DMVA has taken steps to ensure that it obtains complete in-kind assistance information of federal awards from the U.S. Property and Fiscal Office (USPFO).

**Audit Period:** October 1, 2007 through September 30, 2009  
**Finding Number:** 5111003  
**Finding Title:** Revenue Classification

**Finding:** DMVA did not classify certain revenues by the correct revenue source.

**Agency Comments:** Corrective action complete. In fiscal year 2009-10, DMVA corrected revenue objects used for the ChalleNGe Program from the Battle Creek School Aid Fund, the civil service assessment, as well as the Mackinac Bridge Authority Labor Day Bridgewalk services.

Audit Findings Not Corrected or Partially Corrected:

**Audit Period:** October 1, 2005 through September 30, 2007  
**Finding Number:** 5110802F  
**Finding Title:** Federal Reimbursements

**Finding:** DMVA needs to improve its process for requesting federal reimbursement to help ensure timely collection of federal funds. Also, DMVA should request all federal funds available to pay for program operations eligible for federal reimbursement.

**Agency Comments:** Corrective action complete. DMVA has requested advance payments from the Air National Guard Appendixes in addition to the advances it already received for the Army National Guard Appendixes. These advances were for salaries and wages only. However, the process for receiving advances for Air National Guard Appendixes took longer than the reimbursement process. In fiscal year 2011-12, the National Guard Bureau, U.S. Department of Defense, established a new financial, asset, and accounting management system. Its General Fund Enterprise Business System (GFEBS) advance process is cumbersome and does not easily allow for advances. As a result, DMVA will use the reimbursement process for all appendixes of the Master Cooperative Agreement. For construction project payments of \$50,000 or greater, DMVA now releases the vendor payment in the Advanced Purchasing and Inventory Control System (ADPICS), prepares the request for reimbursement (form SF270), and obtains the federal program manager's approval on the same day. This process reduces the time elapsing between the transfer of federal funds and the disbursement of funds by the State.

**Audit Period:** October 1, 2005 through September 30, 2007

**Finding Number:** 5110806F

**Finding Title:** Internal Control Over Procurement

**Finding:** DMVA's internal control did not ensure that it complied with State procurement policies when purchasing some services.

**Agency Comments:** Corrective action complete. With the rollout and implementation of the State of Michigan's on-line bidding system and the requirement effective December 1, 2009 for all bids to be formally placed on this Web site, any vendors who are formally debarred will "not" be able to submit bids through the Web site.

**Audit Period:** October 1, 2007 through September 30, 2009

**Finding Number:** 5111002

**Finding Title:** Federal Reimbursements

**Finding:** DMVA needs to improve its process for requesting federal reimbursement to help ensure timely collection of federal funds.

**Agency Comments:** Corrective action complete. DMVA has requested advance payments from the Air National Guard Appendixes in addition to the advances it already received for the Army National Guard Appendixes. Also, prior to releasing construction project payments of \$50,000 or greater, DMVA now obtains the federal program manager's approval on the request for reimbursement (form SF270). This process allows DMVA to bill the federal government at the same time the payment is being released. This process reduces the time elapsing between the transfer of federal funds and the disbursement of funds by the State.

**Audit Period:** October 1, 2007 through September 30, 2009

**Finding Number:** 5111004

**Finding Title:** Internal Control Over Procurement

**Finding:** DMVA's internal control did not ensure that it complied with State procurement policies when purchasing certain services.

**Agency Comments:** Corrective action complete.

## PRIOR AUDIT FINDINGS RELATED TO FEDERAL AWARDS

### Audit Findings That Have Been Fully Corrected:

**Audit Period:** October 1, 2005 through September 30, 2007  
**Finding Number:** 5110808F  
**Finding Title:** National Guard Military Operations and Maintenance (O&M) Projects, *CFDA* 12.401

**Finding:** DMVA's internal control over the O&M Projects Program did not ensure its compliance with federal laws and regulations and cooperative agreements regarding activities allowed or unallowed, allowable costs/cost principles, period of availability, and procurement and suspension and debarment.

**Agency Comments:** Corrective action complete. A collaborative effort with the federal awarding agency (USPFO), the federal program managers, and DMVA has been initiated, and DMVA has developed a process to address the finding. DMVA is constantly working with the USPFO and other federal program managers to help ensure that all parties understand their duties and responsibilities regarding compliance with final accounting memorandums closing out the grant award year.

**Audit Period:** October 1, 2007 through September 30, 2009  
**Finding Number:** 5111009  
**Finding Title:** Veterans State Domiciliary Care and Veterans State Nursing Home Care, *CFDA* 64.014 and *CFDA* 64.015

**Finding:** DMVA's internal control over the Veterans State Domiciliary Care and Veterans State Nursing Home Care Programs did not ensure its compliance with federal laws and regulations regarding activities allowed or unallowed.

**Agency Comments:** Corrective action complete. GRHV has revised existing administrative policy 11-03-A1 as well as developed a monitor to ensure compliance.

The D.J. Jacobetti Home for Veterans has revised policy 03-05 to clarify the minimum approval required for admission and documentation of this approval.

Audit Findings Not Corrected or Partially Corrected:

**Audit Period:** October 1, 2005 through September 30, 2007

**Finding Number:** 5110807F

**Finding Title:** Military Construction, National Guard, *CFDA* 12.400

**Finding:** DMVA's internal control over the Military Construction, National Guard Program did not ensure its compliance with federal laws and regulations and cooperative agreement requirements regarding allowable costs/cost principles and period of availability.

**Agency Comments:** Corrective action complete. A collaborative effort with the federal awarding agency (USPFO), the federal program manager, and DMVA has been initiated, and DMVA has developed a process to address the finding.

**Audit Period:** October 1, 2005 through September 30, 2007

**Finding Number:** 5110809F

**Finding Title:** National Guard Civilian Youth Opportunities, *CFDA* 12.404

**Finding:** DMVA's internal control over the National Guard Civilian Youth Opportunities Program did not ensure its compliance with federal laws and regulations and cooperative agreements regarding allowable costs/cost principles, period of availability, reporting, and subrecipient monitoring.

**Agency Comments:** Corrective action complete. DMVA obtained semiannual certifications for the audit period. The certifications have been signed by the supervisory official having firsthand knowledge of the work performed by the cadre staff. ChalleNGe Program employees now use the State of Michigan's Data Collection and Distribution System (DCDS) to record their hours worked.

DMVA has updated its desk operating procedures to ensure compliance with period of availability requirements and monthly reporting requirements for the ChalleNGe Program.

Regarding subrecipient monitoring, DMVA has established a procedure to document its annual on-site visits and its monthly review of Starbase reimbursement requests. DMVA has also documented its monitoring process to ensure review of the required audit reports. Discrepancies in the audit reports are investigated, and communication with the subrecipient is established to reconcile the discrepancy.

**Audit Period:** October 1, 2007 through September 30, 2009

**Finding Number:** 5111005

**Finding Title:** Military Construction, National Guard, *CFDA* 12.400

**Finding:** DMVA's internal control over the Military Construction, National Guard Program did not ensure its compliance with federal laws and regulations and cooperative agreement requirements regarding period of availability of federal funds.

**Agency Comments:** Corrective action in process. DMVA is developing formal procedures to ensure timely delivery to the USPFO of a full and final accounting for completed projects. DMVA is currently working with the Construction Facilities Management Office federal program manager and the USPFO to develop joint operating procedures to ensure that the National Guard Bureau form 593-R is properly completed and signed timely.

**Audit Period:** October 1, 2007 through September 30, 2009  
**Finding Number:** 5111006  
**Finding Title:** ARRA - National Guard Military Operations and Maintenance (O&M) Projects, *CFDA* 12.401

**Finding:** DMVA's internal control did not ensure that O&M Projects funded by the American Recovery and Reinvestment Act of 2009 (ARRA) complied with ARRA requirements regarding activities allowed or unallowed, the Davis-Bacon Act, and procurement and suspension and debarment compliance requirements.

**Agency Comments:** Corrective action complete. The appropriate terms and conditions have been included in subsequent contracts funded by ARRA.

**Audit Period:** October 1, 2007 through September 30, 2009  
**Finding Number:** 5111007  
**Finding Title:** National Guard Military Operations and Maintenance (O&M) Projects, *CFDA* 12.401

**Finding:** DMVA's internal control over O&M Projects Program did not ensure compliance with federal laws and regulations regarding activities allowed or unallowed, allowable costs/cost principles, period of availability, and procurement and suspension and debarment.

**Agency Comments:** Corrective action in process. DMVA has established with the USPFO a process for initial funding, modifications, and closeouts. DMVA monitors each appendix to determine if the maximum funding limitation is exceeded and notifies the program manager and the USPFO. DMVA has submitted to the USPFO a Centralized Personnel Plan to allocate the direct cost of staff to the appropriate agreement appendix. Because DMVA's Centralized Personnel Plan is still under review by the USPFO, this finding is categorized as partially corrected.

**Audit Period:** October 1, 2007 through September 30, 2009  
**Finding Number:** 5111008  
**Finding Title:** National Guard Civilian Youth Opportunities, *CFDA* 12.404

**Finding:** DMVA did not comply with National Guard Civilian Youth Opportunities (NGCYO) Program federal laws and regulations and cooperative agreements concerning eligibility. Also, DMVA's internal control over the NCGYO Program did not ensure its compliance with federal laws and regulations and cooperative agreements regarding reporting and subrecipient monitoring.

**Agency Comments:** Corrective action complete. Regarding eligibility, at the time DMVA accepts the applicants, they are dropouts. Regarding subrecipient monitoring, DMVA is documenting its annual on-site visit and its monthly review of Starbase requests for reimbursement. DMVA has established a process to ensure review of the Starbase annual audit report and reconciling any discrepancy with Starbase.

DEPARTMENT OF MILITARY AND VETERAN'S AFFAIRS

Corrective Action Plan

As of June 7, 2012

**FINDINGS RELATED TO THE FINANCIAL STATEMENTS**

**Finding Number:** 5111201  
**Finding Title:** Schedule of Expenditures of Federal Awards (SEFA)

**Management Views:** The Department of Military and Veterans Affairs (DMVA) concurs with the audit finding. DMVA has made significant improvements in SEFA preparation. Being deliberate and careful, it is always DMVA's intent to achieve perfection. DMVA believes that reasonable internal control has been implemented. DMVA is committed to further strengthening its internal control.

**Planned Corrective Action:** Prior to submission, DMVA has a final review of the SEFA performed by a knowledgeable person independent of the schedule preparation to ensure that the SEFA is as accurate and complete as possible.

**Anticipated Completion Date:** December 2012

**Responsible Individual:** Alfred E. Christian, Interim Chief Financial Officer

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**Finding Number:** 5111202  
**Finding Title:** Capital Asset Reporting

**Management Views:** DMVA concurs with the audit finding that it did not report all capital asset disposals and did not report all its capital assets to the Office of Financial Management (OFM), Department of Technology, Management, and Budget (DTMB), during the audit period.

**Planned Corrective Action:** DMVA will properly report to OFM the capital asset disposals and the value of the six armories and one parcel of armory land in fiscal year 2011-12 in accordance with the State of Michigan Financial Management Guide (Part II, Chapter 21, Section 220).

**Anticipated Completion Date:** November 2012

**Responsible Individual:** LTC Stephen J. Ward, Director, Construction and Facilities Management Office

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**Finding Number:** 5111203

**Finding Title:** Revenue Classification

**Management Views:** DMVA concurs with the audit finding that DMVA did not classify private medical insurance revenues by the correct revenue source. DMVA is committed to strengthening its internal control and will institute the procedures to resolve this issue.

**Planned Corrective Action:** DMVA will classify private medical insurance revenues appropriately utilizing the comptroller object and agency object of 1555 ("1<sup>st</sup> & 3<sup>rd</sup> Party Reimbursement - Services"). DMVA will, at least annually, prepare a journal entry to move the revenue to the Income and Assessments Fund. DMVA will make this process a part of its year-end closing checklist. The process will begin in fiscal year 2011-12.

**Anticipated Completion Date:** November 2012

**Responsible Individual:** Alfred E. Christian, Interim Chief Financial Officer

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**Finding Number:** 5111204  
**Finding Title:** Cash Management

**Management Views:** DMVA concurs with the audit finding.

The audit finding (part a.(1)) states that DMVA has not submitted requests for 22 expenditures. To say that reimbursement was not requested at all or not in a timely manner is misleading. DMVA requested reimbursement for all expenditures; however, DMVA was not reimbursed in a timely manner. DMVA prepared and submitted the reimbursement requests to the Construction and Facilities Management Office (CFMO) federal program manager. The responsibility for certifying payment requests as well as making sure the funding is in the proper federal accounts rests with the federal program manager. The State's responsibility is to present a properly documented and prepared request. DMVA performed its responsibilities and is awaiting CFMO approval and submission to the U.S. Property and Fiscal Office (USPFO) for reimbursement.

**Planned Corrective Action:** DMVA has engaged its federal program managers as well as the USPFO and will continue to seek ways to further minimize the time elapsing between the transfer of federal funds and the disbursement of funds by the State.

**Anticipated Completion Date:** October 2012

**Responsible Individual:** Alfred E. Christian, Interim Chief Financial Officer

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**Finding Number:** 5111205  
**Finding Title:** Procurement

**Management Views:**

DMVA concurs with audit finding 5111207, part c., Davis-Bacon Act.

DMVA disagrees with audit finding 5111208, part c.(1) relating to the Starbase, Inc. grant agreement and related questioned costs of \$4,191,931. A grant agreement was developed by the DMVA Judge Advocate General between DMVA and Starbase, Inc. in 1997 and that model continues to be used today.

DMVA concurs with audit finding 5111208, part c.(2).

DMVA has established procedural enhancements to include verification that the contracting entity is not suspended, debarred, or otherwise excluded from participating in federal or State programs by checking the Excluded Parties List System. All suspension and debarment searches will be kept on file.

**Planned Corrective Action:**

5111207, part c., Davis-Bacon Act - When legislation exists concerning the Davis-Bacon Act and Buy American, DMVA will ensure that DTMB includes the aforementioned language in DMVA's contracts.

5111208, part c.(2), National Guard Challenge Program - DMVA has established procedural enhancements to include verification that the contracting entity is not suspended, debarred, or otherwise excluded from participating in federal or State programs by checking the Excluded Parties List System. All suspension and debarment searches will be kept on file.

**Anticipated Completion Date:** June 2012

**Responsible Individual:** Alfred E. Christian, Interim Chief Financial Officer

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## FINDINGS RELATED TO FEDERAL AWARDS

**Finding Number:** 5111206  
**Finding Title:** Military Construction, National Guard, *CFDA* 12.400

**Management Views:** DMVA concurs with the audit finding.

The audit finding states that "DMVA did not deliver to the NGB full and final accountings liquidating all payments or reimbursements within 90 days of the final completion for all 5 projects reviewed or obtain the NGB's approval to extend the 90-day limit." While technically correct, the CFMO completed quarterly meetings with the USPFO to ensure that all accounts were properly obligated and liquidated. These meetings ensure that no changes occur after the NGB form 593R is signed. The CFMO simply did not inform State Operations to write an extension letter in a timely manner, even though the accounting had been completed. There were no new obligations made after the 90-day limit, only liquidations.

**Planned Corrective Action:** Internal control will be put in place to ensure that State Operations receives NGB form 593R in a timely manner so that, if an extension is needed, it can then be requested. The CFMO will continue with its hands-on meetings with the USPFO to ensure that obligations are all accounted for in accordance with the regulation.

**Anticipated Completion Date:** September 2012

**Responsible Individual:** LTC Stephen J. Ward, Director, Construction and Facilities Management Office

- Finding Number:** 5111207
- Finding Title:** National Guard Military Operations and Maintenance (O&M) Projects and ARRA - National Guard Military Operations and Maintenance (O&M) Projects, *CFDA* 12.401
- Management Views:**
- a. Activities Allowed or Unallowed - DMVA concurs with the audit finding.
  - b. Allowable Costs/Cost Principles - DMVA concurs with the audit finding. The original time sheets were lost and it was unable to locate the documentation after many attempts.
  - c. Davis-Bacon Act - DMVA's corrective action plan from the prior audit did allow DMVA to monitor future American Recovery and Reinvestment Act of 2009 (ARRA) contracts and Davis-Bacon Act language was included in subsequent contracts, but DMVA was unable to amend previously approved contracts without the consent of the contractors.
  - d. Procurement and Suspension and Debarment - DMVA will ensure that Buy American language is included in construction contracts when required.
- Planned Corrective Action:**
- a. Activities Allowed or Unallowed - Appendix 28 has become a Special Military Cooperative Agreement effective October 1, 2011.
  - b. Allowable Costs/Cost Principles - DMVA will establish a policy for those timekeeping units in which time sheets were maintained on site (due to employees not entering their own time in the Data Collection and Distribution System [DCDS]),

requesting those records be sent annually to the Office of Human Resources where they will be maintained in accordance with State of Michigan records retention and disposal schedules.

- c. Davis-Bacon Act - When legislation exists concerning the Davis-Bacon Act and Buy American, DMVA will ensure that DTMB includes the aforementioned language in DMVA's contracts.
- d. Procurement and Suspension and Debarment - DMVA will ensure that Buy American language is included in construction contracts when required.

- Anticipated Completion Date:**
- a. Activities Allowed or Unallowed - Corrective action was completed October 2011 with the establishment of the Special Military Cooperative Agreement.
  - b. Allowable Costs/Cost Principles - October 2012
  - c. Davis-Bacon Act - June 2012
  - d. Procurement and Suspension and Debarment - October 2011

**Responsible Individual:** Alfred E. Christian, Interim Chief Financial Officer

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**Finding Number:** 5111208

**Finding Title:** National Guard ChalleNGe Program, CFDA 12.404

- Management Views:**
- a. Eligibility - DMVA concurs with the audit findings related to the ChalleNGe Program.

- b. Matching, Level of Effort, and Earmarking - DMVA concurs with the audit findings.
- c. Procurement and Suspension and Debarment - DMVA disagrees with the audit finding relating to the Starbase, Inc. grant agreement and related questioned costs of \$4,191,931.

DMVA agrees that it did not obtain State Administrative Board approval and did not competitively bid the procurement. DMVA has a longstanding relationship with Starbase, Inc. A grant agreement was developed by the DMVA Judge Advocate General between DMVA and Starbase, Inc. in 1997 and that model continues to be used today. This program has been audited annually by a private audit firm, the Office of the Auditor General (through single audits), and USPFO-Internal Review. None of these audits have questioned the validity of the grant agreement. Because Starbase, Inc., a nonprofit organization, initiated this innovative program, created the objectives by which the program would be analyzed and deemed successful, and was qualified and competent, DMVA has not sought to competitively bid this grant.

- d. Reporting - DMVA concurs with the audit finding. During the audit period, only one staff person was responsible for generating more than 80 reimbursement requests per month for Master Cooperative Agreement appendixes, Minor Construction Cooperative Agreements, Homeland Security Grants and National Guard Challenge Program grants.

- Planned Corrective Action:**
- a. Eligibility - Beginning with the July 2012 class, new procedures will be initiated to ensure compliance with all ChalleNGe Program requirements. Records for each applicant/student will reflect his or her status in all areas and these records will be safeguarded to prevent loss or damage.
  - b. Matching, Level of Effort, and Earmarking - Effective January 2012, DMVA will no longer apply Title I funds received from the Battle Creek Public School District to meet State matching requirements.
  - d. Reporting - Additional staff were hired in August 2011. Allowing for adequate training, DMVA anticipates that compliance with reporting requirements will be in place by July 2012.

- Anticipated Completion Date:**
- a. Eligibility - July 2012
  - b. Matching, Level of Effort, and Earmarking - January 2012
  - d. Reporting - August 2012

**Responsible Individual:** Alfred E. Christian, Interim Chief Financial Officer

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# GLOSSARY

## Glossary of Acronyms and Terms

adverse opinion	An auditor's opinion in which the auditor states that the audited entity did not comply, in all material respects, with the cited requirements that are applicable to each major federal program.
American Recovery and Reinvestment Act of 2009 (ARRA)	An economic stimulus package enacted by the 111th United States Congress in February 2009.
<i>Catalog of Federal Domestic Assistance (CFDA)</i>	The catalog that provides a full listing, with detailed program descriptions, of all federal programs available to state and local governments.
CFMO	Construction and Facilities Management Office.
<i>Code of Federal Regulations (CFR)</i>	The codification of the general and permanent rules published by the departments and agencies of the federal government.
deficiency in internal control over federal program compliance	The design or operation of a control over compliance that does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis.
deficiency in internal control over financial reporting	The design or operation of a control that does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis.
DJJHV	D.J. Jacobetti Home for Veterans.
DMVA	Department of Military and Veterans Affairs.

DTMB	Department of Technology, Management and Budget.
financial audit	An audit that is designed to provide reasonable assurance about whether the financial statements of an audited entity are presented fairly in all material respects in conformity with the disclosed basis of accounting.
form 593R	project inspection report.
generally accepted accounting principles (GAAP)	A technical accounting term that encompasses the conventions, rules, guidelines, and procedures necessary to define accepted accounting practice at a particular time; also cited as "accounting principles generally accepted in the United States of America."
Governmental Accounting Standards Board (GASB)	An arm of the Financial Accounting Foundation established to promulgate standards of financial accounting and reporting with respect to activities and transactions of state and local governmental entities.
GRHV	Grand Rapids Home for Veterans.
in-kind assistance	The value of a noncash contribution by a nonfederal third party without charge to the grantee or a cost-type contractor of supplies, equipment, goods, property, and services, directly benefiting and specifically identifiable to a federal program.
internal control	A process, effected by those charged with governance, management, and other personnel, designed to provide reasonable assurance about the achievement of the entity's objectives with regard to the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

low-risk auditee	As provided for in OMB Circular A-133, an auditee that may qualify for reduced federal audit coverage if it receives an annual single audit and it meets other criteria related to prior audit results. In accordance with State statute, this single audit was conducted on a biennial basis; consequently, this auditee is not considered a low-risk auditee.
material misstatement	A misstatement in the financial statements that causes the statements to not present fairly the financial position or the changes in financial position or cash flows in conformity with the disclosed basis of accounting.
material noncompliance	Violations of laws, regulations, contracts, and grants that could have a direct and material effect on major federal programs or on financial statement amounts.
material weakness in internal control over federal program compliance	A deficiency, or a combination of deficiencies, in internal control over compliance such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.
material weakness in internal control over financial reporting	A deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the financial statements will not be prevented, or detected and corrected, on a timely basis.
MCA	Master Cooperative Agreement.
MCCA	Military Construction Cooperative Agreement.
MYPCA	Master Youth Programs Cooperative Agreement.
NGB	National Guard Bureau.

NGC Program	National Guard Challenge Program.
NGCYO	National Guard Civilian Youth Opportunities.
O&M	National Guard Military Operations and Maintenance.
OFM	Office of Financial Management.
other noncompliance	Violations of contracts or grant agreements that are not material to the financial statements but should be communicated to management in accordance with <i>Government Auditing Standards</i> . Other noncompliance also includes violations of laws, regulations, contracts, or grant agreements; fraud; abuse; or other internal control deficiencies that may be communicated to management in accordance with <i>Government Auditing Standards</i> .
pass-through entity	A nonfederal entity that provides a federal award to a subrecipient to carry out a federal program.
questioned cost	A cost that is questioned by the auditor because of an audit finding: (1) which resulted from a violation or possible violation of a provision of a law, regulation, contract, grant, cooperative agreement, or other agreement or document governing the use of federal funds, including funds used to match federal funds; (2) where the costs, at the time of the audit, are not supported by adequate documentation; or (3) where the costs incurred appear unreasonable and do not reflect the actions a prudent person would take in the circumstances.
SEFA	schedule of expenditures of federal awards.

significant deficiency in internal control over federal program compliance	A deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.
significant deficiency in internal control over financial reporting	A deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.
single audit	A financial audit, performed in accordance with the Single Audit Act Amendments of 1996, that is designed to meet the needs of all federal grantor agencies and other financial report users. In addition to performing the audit in accordance with the requirements of auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in <i>Government Auditing Standards</i> issued by the Comptroller General of the United States, a single audit requires the assessment of compliance with requirements that could have a direct and material effect on a major federal program and the consideration of internal control over compliance in accordance with OMB Circular A-133.
<i>SOMCAFR</i>	<i>State of Michigan Comprehensive Annual Financial Report.</i>
subrecipient	A nonfederal entity that expends federal awards received from another nonfederal entity to carry out a federal program.
unqualified opinion	<p>An auditor's opinion in which the auditor states that:</p> <ol style="list-style-type: none"> <li>a. The financial statements presenting the basic financial information of the audited entity are fairly presented in conformity with the disclosed basis of accounting; or</li> </ol>

- b. The financial schedule and/or financial statement presenting supplemental financial information are fairly stated in relation to the basic financial statements. In issuing an "in relation to" opinion, the auditor has applied auditing procedures to the supplemental financial schedule and/or financial statement to the extent necessary to form an opinion on the basic financial statements, but did not apply auditing procedures to the extent that would be necessary to express an opinion on the supplemental financial schedule and/or financial statement taken by themselves; or
- c. The audited entity complied, in all material respects, with the cited requirements that are applicable to each major federal program.

U.S. Office of  
Management and  
Budget (OMB)

A cabinet-level office that assists the President in overseeing the preparation of the federal budget and in supervising its administration in executive branch agencies.

USPFO

U.S. Property and Fiscal Office.







