



City of Chattanooga

Stan Sewell
Director

INTERNAL AUDIT
City Hall
Chattanooga, Tennessee 37402

Ron Littlefield
Mayor

March 22, 2012

Mayor and City Council
City of Chattanooga
Chattanooga, TN 37402

RE: Police Special Investigations Funds, Audit 11-11

Dear Mayor Littlefield and City Council Members:

Attached is the Internal Audit Division's report on Police Special Investigations Funds, Audit 11-11.

The Police department has already taken positive actions in response to our findings and recommendations. We thank the management and staff of the Police and Finance department for their cooperation and assistance during this audit.

Sincerely,

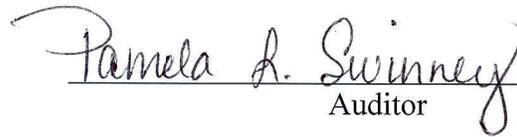
Stan Sewell, CPA, CGFM
Director of Internal Audit

Attachment

cc: Audit Committee Members
Dan Johnson, Chief of Staff
Daisy Madison, Finance Administrator
Bobby Dodd, Chief of Police
Tim Carroll, Assistant Chief of Investigative Services

**POLICE DEPARTMENT
SPECIAL INVESTIGATIONS FUNDS
AUDIT 11-11
FEBRUARY 28, 2012**

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Auditor



Audit Director

**POLICE DEPARTMENT
SPECIAL INVESTIGATIONS FUNDS
AUDIT 11-11**

INTRODUCTION

The Major Narcotics and Vice Section (Narcotics & Vice) is a component of the Special Investigations Unit within the Criminal Investigations Command. Narcotics & Vice officers conduct covert operations for the control of vice, narcotics, and organized crime violations.

To support the division's undercover operations, the department utilizes confidential funds. Confidential fund expenditures must adhere to the Comptroller's guide for cash transactions related to undercover operations. These minimum guidelines, along with departmental policies (SOP-1) developed by Chattanooga Police Department (CPD), apply only to those transactions which, for confidentiality reasons, must be disbursed in cash for covert operations. Examples of these expenditures include:

- Payments made to an informant for information are reported and witnessed on Form A-5;
- Payments made to an independent undercover agent are reported and witnessed on Form A-5);
- Money spent to actually purchase drugs as part of an undercover operation are reported and witnessed on Form A-5;
- Gasoline or minor maintenance for an undercover vehicle or informant's vehicle when used in undercover operations is reported on Form A-4, with receipts attached.

Because funds cannot be distributed to officers directly from the City's general fund, CPD has two confidential fund checking accounts for undercover operations: Narcotics and Part I Offenses. The department uses the same policies and procedures for both confidential funds. As required by State code, all expenditures from the narcotics confidential checking account are for drug-related undercover operations. Part I Offenses confidential checking account is used for all other types of undercover operations (i.e. prostitution, burglary, homicide, organized crime).

T.C.A. 39-17-420 establishes the Drug Fund special revenue account (Drug Fund) and places it under the control of the city recorder. All financial activities related to funds received under this section must be accounted for in the special revenue fund.

There are several sources of revenue for the Drug Fund. All fines from drug offenses must be turned over to the local government of the arresting agency. T.C.A. 39-17-428 requires that 50 percent of each fine go to the city's General Fund and 50 percent to the city's Drug Fund special revenue account. Any cash that is forfeited to the city as well as the proceeds from the sale of any forfeited property go into the Drug Fund. Other sources of revenue can include donations and appropriations from the local governing body.

T.C.A. 39-17-420 allows expenditures from the Drug Fund for local drug enforcement programs, local drug education programs, local drug treatment programs and nonrecurring general law enforcement expenditures. All expenditures, with the exception of confidential fund expenditures, must follow the city’s purchasing guidelines. The fund for confidential expenditures is actually a separate checking account under the control of the police chief or his designee. Funds for the confidential account are requested from the City Finance Officer, and then deposited in the confidential checking account.

STATISTICS

<u>Special Revenue Fund - Narcotics</u>	<u>FY11</u>	<u>FY10</u>
Travel	\$ 9,488	\$ 7,250
Machinery & Equipment	\$ 285,260	\$ 70,120
Confidential Expenditures	\$ 80,609	\$ 139,492
Supplies and Services	<u>\$ 60,685</u>	<u>\$ 54,988</u>
Total Expenditures	<u>\$ 436,042</u>	<u>\$ 271,856</u>

Source: CPD’s Annual Report of Municipal Narcotic Drug Fund Activities

STATEMENT OF OBJECTIVES

This audit was conducted in accordance with the Internal Audit Division's 2011 Audit Agenda. The objectives of this audit were to determine if:

1. Expenditures from the Drug Fund comply with applicable laws; and
2. Confidential funds were administered in accordance with established policies and procedures.

STATEMENT OF SCOPE

Based on the work performed during the preliminary survey and the assessment of risk, the audit will cover confidential funds from July 1, 2010 to October 31, 2011. Source documentation was obtained from Police and Finance departments. Original records as well as copies were used as evidence and verified through physical examination.

STATEMENT OF METHODOLOGY

During the audit, interviews were conducted with Police and Finance department staff. We reviewed the Police department’s policies related to fiscal procedures (SOP-1), confidential informants (SOP-3), and confiscated property (OPS-17). In addition, we reviewed *Internal Control and Compliance Manual for Tennessee Municipalities, Procedures for Handling*

Cash Transactions Related to Undercover Investigative Operations of County and Municipal Drug Enforcement Programs, Chattanooga City Code and Charter, and Tennessee Code Annotated for pertinent facts related to our audit.

We obtained records from the Police department to determine if proper purchasing procedures were followed related to expenditures from the Narcotics Special Revenue Fund. We reviewed a sample of closed case files to verify confidential expenditures were in accordance with all applicable laws and policies.

The sample size and selection were statistically generated using a desired confidence level of 90 percent, expected error rate of 5 percent, and a desired precision of 5 percent. Statistical sampling was used in order to infer the conclusions of test work performed on a sample to the population from which it was drawn and to obtain estimates of sampling error involved. When appropriate, judgmental sampling was used to improve the overall efficiency of the audit.

STATEMENT OF AUDITING STANDARDS

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

AUDIT CONCLUSIONS

Based upon the test work performed and the audit findings noted below, we conclude that:

1. Expenditures from the Drug Fund complied with applicable laws; and
2. Confidential funds were administered in accordance with established policies and procedures; however, additional safeguards are needed.

While the findings discussed below may not, individually or in the aggregate, significantly impair the operations of the Investigative Services division, they do present risks that can be more effectively controlled.

FINDINGS AND RECOMMENDATIONS

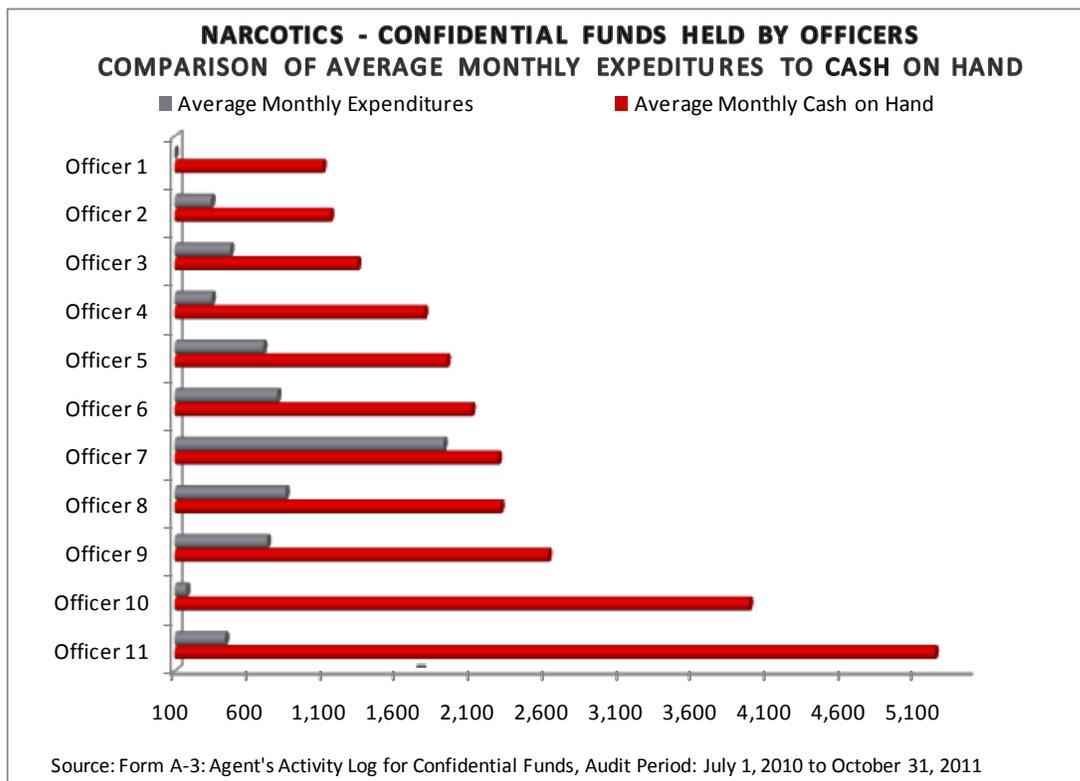
The Narcotics and Vice division have excess cash on hand for confidential operations.

The State Comptroller's confidential funds policies does not specifically place limits on the amount of cash held by undercover investigators and/or Police personnel. However, the manual recommends the initial deposit to the confidential funds checking account not exceed 45 days of need.

Our review of the department’s policies and procedures found no established criteria to determine and/or estimate each officer’s cash requirements to facilitate undercover operations. We reviewed sixteen (16) months of confidential fund transactions to establish average monthly expenditures by officers. Our analysis indicates the department keeps excess cash on hand for both Narcotics and Vice undercover operations.

Narcotics – Confidential Funds

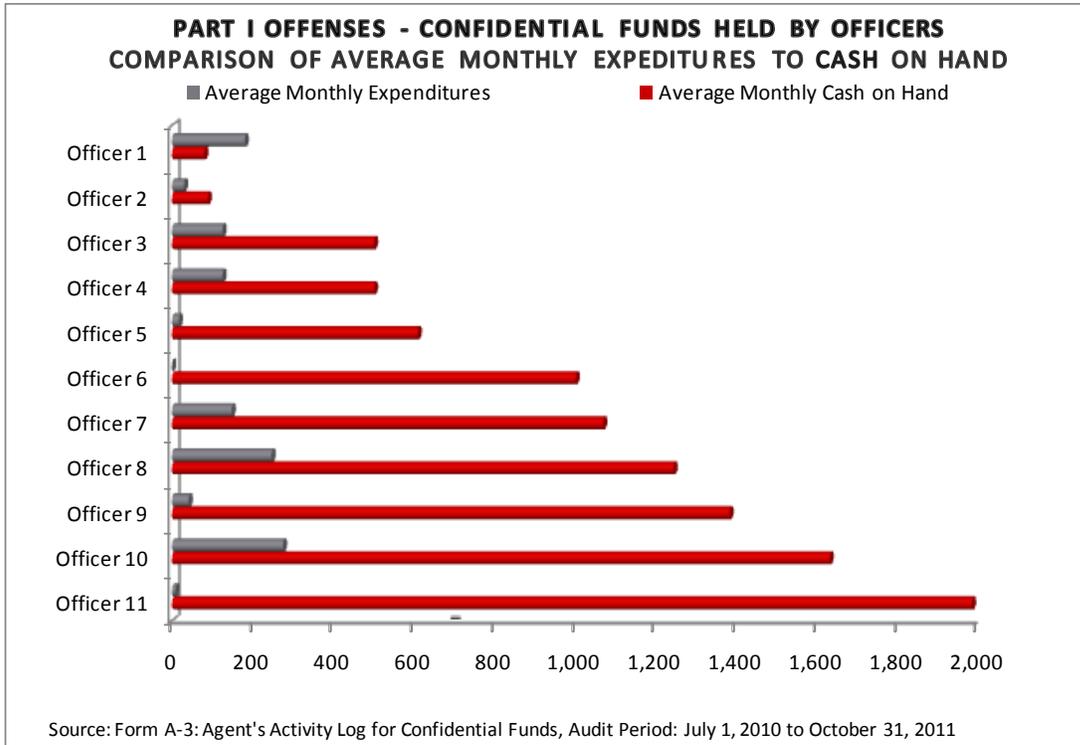
As depicted in the chart below, we found eleven (11) narcotics officers held confidential funds during the audit period. Cash on hand exceeded three (3) times their average monthly expenditures. We noted one narcotics officer (Officer 1) held over \$1,000 during a 15 month period but had no undercover operational expenditures. The remaining 10 narcotics officers had total monthly average cash on hand of \$18,400 but only spent an average total of \$6,700 a month for undercover operations. Only one of the eleven officers (Officer 7) appears to maintain cash on hand relative to monthly expenditures.



Confidential Funds – Part I Offenses (Vice)

As depicted in the chart below, we found eleven (11) officers held Part I confidential funds during the audit period. Cash on hand exceeded seven (7) times their average monthly expenditures. We found Officer 6 held over \$1,000 with no expenditures during the audit period and Officer 11 had \$2,000 but made only one \$15 expenditure during a 14 month period. Of the eleven (11) officers that held Part I funds during the audit period, we noted

only four (4) officers that made regular expenditures. We found these four officers had a monthly average of \$5,300 in cash on hand but only spent an average of \$710 a month during the audit period.



Recommendation 1

We recommend the Police department develop and implement procedures for determining the amount of confidential funds necessary per officer. Further, we recommend periodic review of the established criteria to ensure cash held by officers is not excessive.

Auditee Response

The Special Investigations supervisors will evaluate, on a monthly basis, the amount of confidential funds held by each investigator. This evaluation will be completed by comparing the amount of funds utilized during the month against the amount of funds the investigators have in their possession. While it is difficult to place an exact figure on a reasonable amount to be maintained, in general, that amount should not exceed \$1000 more than the average monthly expenditures of the investigators.

The Narcotics and Vice Section should implement additional policies and procedures.

Overall, the departments policies and procedures for confidential cash expenditures properly address the minimum controls required by the Comptroller's *Procedures for Handling Cash Transactions Related to Undercover Investigative Operations of County and Municipal Drug Enforcement Programs*. However, during the audit, we found the organization and retention of case files and confidential forms does not facilitate an adequate review process.

Consistent Use of Case Numbers on Forms: The confidential expenditure forms include a field to list the case number. We examined a sample of documents and noted inconsistent practice among officers. We found officers would inconsistently use the narcotics/vice case number, the RMS computer-generated complaint number, or omit the number. Currently, the department's policies do not require a consistent use of the Narcotics/Vice assigned case number for all support documents.

Records Retention and Organization: The Comptroller's procedure manual allows audit of Form A-4 (Accountability of Confidential Funds) once the case is closed. We found the confidential expenditure forms (A-4, A-5) are not maintained with the case files due to open records request protection. Instead, the original copies are filed by the log custodian by month of expenditure. The log custodian receives no information related to the status of cases. Also, the officer is required to maintain a copy of the confidential forms which are typically filed in their respective filing cabinets and/or desk drawers. Confidential expenditure forms should be filed by case number to facilitate both supervisor reviews and the annual audit required by the department's SOP-1.

Investigative Report Content: We reviewed a sample of closed case files and found the investigative report content varies by officer. We noted officers did not always include names of other officers present during operations; thereby, reducing the reviewers' ability to verify witness signatures on the A-5 forms. Currently, the department's policies do not provide guidance related to investigative report content.

The current system requires gathering information from several areas to verify the case records are valid and expenditures are reasonable. The consistent use of case numbers, adequate investigative report content, and a centralized filing system of confidential forms would facilitate the review process. These additional procedures could help detect errors and fraud as well as limit opportunity for theft and/or unauthorized use of assets.

Recommendation 2

We recommend the Police department implement the additional policies and procedures discussed above and include the new procedures in its SOP manual.

Auditee Response

Consistent use of case numbers

The investigative supervisors will maintain an electronic log for the assignment of case numbers. These case numbers will be issued sequentially preceded by the last two digits of the current year. The supervisors will enter information pertinent to the investigation including, but not limited to: requesting investigator, date opened, date closed, status of case. These case numbers will then be used and recorded on all documentation related to a particular case. This will include records of confidential fund expenditures, informant payments, undercover evidence purchases, CPD incident reports, and investigator's field notes.

Records retention and organization

Each investigator will maintain an updated case file on all open investigations. At the conclusion of the investigation the completed file will be submitted to the investigative supervisor for review/approval. The investigator will also maintain a separate, but associated, case file containing A-4's and A-5's related to a particular case. This file will also be submitted to the investigative supervisor for his review/approval of the case file. Upon approval the associated case file containing the A-4/A-5 copies will be returned to the investigator for retention in their personal files. This will be done in addition to the monthly report to the log custodian.

Investigative report content

Investigators will maintain updated and complete records, reports, and field notes. All pertinent information related to an investigation should be recorded. Officers' field notes will include all personnel present during any operation. This should also indicate the roles of each of the officers present.

The Narcotics and Vice division has not performed unannounced, random cash counts of officer's confidential funds.

Based on discussion with staff, we learned the division does not perform random cash counts to verify confidential funds held by officers. It appears officers individually perform self checks of their cash on hand each month when completing the "Agent's Monthly Activity Log." Further, the department has no policy or procedure in place requiring cash counts of officer's confidential funds.

The lack of unannounced cash counts coupled with excessive amounts of cash on hand provides greater opportunity for theft or unauthorized use of assets.

Recommendation 3

We recommend the department perform random, annual cash counts of confidential funds held by officers and verify to support documents. Upon request by the Chief of Police, Internal Audit will perform the cash counts as part of its annual petty cash count special project.

Auditee Response

Supervisors will conduct random and unannounced audits of confidential funds held by investigators. A count will be made of the investigator's cash on hand and this will be compared to the current month's expenditure report/balance. Any discrepancy will be immediately investigated to determine the source of any shortage/overage. Supervisors will document these audits through the use of a log that will notate the specifics of the inspection including but not limited to: date/time, investigator, amount on balance sheet, amount present at count.

Currently, the Police department policies require a Finance department staff to sign all checks written from the confidential funds checking account.

The purpose of a separate confidential fund checking account is to provide immediate and confidential access to funds for undercover law enforcement activities. Per *Procedures for Handling Cash Transactions Related to Undercover Investigative Operations of County and Municipal Drug Enforcement Programs*, all disbursements of confidential funds must be by pre-numbered check and “**shall** be signed by the Chief Law enforcement official or his designee.” Further, MTAS’ *Drug Fund Manual* states “the fund for confidential expenditures is actually a separate account **under the control of the police chief or his or her designee.**” [Emphasis Added]

Currently, the confidential funds policy requires both the Police Chief and Finance Accounting Manager to sign all checks written to undercover officers. Typically, due to immediate needs, the undercover officer brings the check to City Hall to obtain the signature. Although the two signature requirement improves controls over the City's assets, giving signatory responsibility to staff outside the Police department is inefficient, unnecessary and compromises the officers' identities.

Recommendation 4

We recommend Finance department be removed from signatory responsibilities on the confidential funds checking accounts. Further, we recommend the Police Chief establish a policy to designate an individual to sign checks (written from the confidential funds accounts), and to provide a threshold amount requiring dual signatures (with Police Chief).

Auditee Response

In line with the suggestions from the auditor, I would recommend the following, deferring to the command staff for approval.

The confidential fund checking account should maintain a minimum balance of \$20,000. The primary signatory responsibilities would rest with the Chief of Police or his designee(s). I suggest the Assistant Chiefs as well as Mike Evans be designated with signatory responsibility. Checks issued in an amount greater than \$5000 require the signatures of two of the parties listed above.