

Audit Report

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**Military Department**

June 2020

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**OFFICE OF LEGISLATIVE AUDITS**  
DEPARTMENT OF LEGISLATIVE SERVICES  
MARYLAND GENERAL ASSEMBLY

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DEPARTMENT OF LEGISLATIVE SERVICES  
OFFICE OF LEGISLATIVE AUDITS  
MARYLAND GENERAL ASSEMBLY

Victoria L. Gruber  
Executive Director

Gregory A. Hook, CPA  
Legislative Auditor

June 10, 2020

Senator Clarence K. Lam, M.D., Senate Chair, Joint Audit and Evaluation Committee  
Delegate Carol L. Krimm, House Chair, Joint Audit and Evaluation Committee  
Members of Joint Audit and Evaluation Committee  
Annapolis, Maryland

Ladies and Gentlemen:

We have conducted a fiscal compliance audit of the Military Department for the period beginning July 1, 2015 and ending May 20, 2019. The Department performs various functions for the public, including maintaining Maryland National Guard locations, coordinating disaster plans to help mitigate future disasters, and administer grants and loans to Volunteer Fire Companies for facilities and equipment.

Our audit disclosed that the Department did not submit requests for reimbursement of federal fund expenditures in a timely manner. In addition, the Department artificially divided purchases of certain equipment maintenance services into multiple procurements and inflated the value of certain purchase orders. Furthermore, supervisory reviews of adjustments to leave balances were not documented and were not performed by an independent employee.

Our audit also included a review to determine the status of the two findings contained in our preceding audit report. We determined that the Department satisfactorily addressed one of the two findings. The remaining finding is repeated in this report.

The Department's response to this audit is included as an appendix to this report. We reviewed the response and noted general agreement to our findings and recommendations, and while there are other aspects of the Department's response which will require further clarification, we do not

anticipate that these will require the Joint Audit and Evaluation Committee's attention to resolve.

We wish to acknowledge the cooperation extended to us during the audit by the Department and its willingness to address the audit issues and implement appropriate corrective actions.

Respectfully submitted,

A handwritten signature in black ink that reads "Gregory A. Hook". The signature is written in a cursive style with a large, prominent initial "G".

Gregory A. Hook, CPA  
Legislative Auditor

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\* Denotes item repeated in full or part from preceding audit report

## **Background Information**

### **Agency Responsibilities**

The Military Department maintains the Maryland National Guard within the State of Maryland, including its 31 readiness centers and numerous other facilities used by the Army and Air National Guard. In addition, the Department, through its Maryland Emergency Management Agency (MEMA), coordinates Statewide efforts in the event of emergencies and disasters that are beyond the capabilities of local authorities. MEMA also coordinates disaster preparedness activities with its federal and local counterparts and, through mitigation services, strives to reduce or eliminate the impact of future disasters. The Department also administers loan and grant programs that provide funding to volunteer fire companies for facilities and equipment.

According to the State's records, during fiscal year 2019, the Department's operating expenditures totaled approximately \$89.0 million, consisting of federal fund expenditures of \$53.6 million, general fund expenditures of \$13.5 million, special fund expenditures of \$21.4 million, and reimbursable fund expenditures of \$494,600.

### **Distribution to Volunteer Company Assistance Fund**

State law established the Volunteer Company Assistance Fund to provide loans and grants to volunteer fire companies. According to the State's records, as of June 30, 2019, the fund balance totaled approximately \$32.2 million consisting of notes receivable due from volunteer fire companies totaling \$21.1 million and cash totaling \$11.1 million.

### **Status of Findings From Preceding Audit Report**

Our audit included a review to determine the status of the two findings contained in our preceding audit report dated March 9, 2016. As disclosed in the table below, we determined that the Department satisfactorily addressed one of the findings. The remaining finding is repeated in this report.

### Status of Preceding Findings

<b>Preceding Finding</b>	<b>Finding Description</b>	<b>Implementation Status</b>
Finding 1	The Military Department did not submit requests for reimbursement of federal fund expenditures in a timely manner.	<b>Repeated</b> (Current Finding 1)
Finding 2	Adequate controls and records were not maintained for MEMA equipment.	Not Repeated

# Findings and Recommendations

## Federal Funds

### **Finding 1**

**The Military Department did not always submit requests for reimbursement of federal fund expenditures in a timely manner.**

### **Analysis**

The Department did not always submit requests for reimbursement of federal fund expenditures related to Maryland Emergency Management Agency (MEMA), primarily related to funding for federally declared disasters, and National Guard Bureau (NGB) grants in a timely manner. Federal guidelines for these grants permit reimbursements to be requested when expenditures are incurred.

According to the State's records, during fiscal year 2019, MEMA and NGB grant expenditures totaled \$18.4 million and \$34.6 million, respectively.

Our test of 10 NGB grant reimbursement requests totaling \$4.7 million processed during fiscal years 2017 through 2019 disclosed that 6 requests totaling \$3.1 million were submitted between 98 and 334 days after the expenditures were incurred. For example, one request for reimbursement of \$1.3 million that was spent during November 2018 was not submitted until March 2019. Similarly, our test of 10 requests for MEMA grant funds totaling \$11.7 million processed during fiscal years 2016 through 2019 disclosed that two requests totaling \$1.9 million were submitted 117 to 125 days after the related expenditures were incurred. A third request totaling \$600,000 had still not been submitted as of the time of our review, which was 407 days after the expenditures were incurred.

The untimely recovery of these funds resulted in lost interest income to the State totaling at least \$9,500. A similar condition was noted in our preceding audit report.

### **Recommendation 1**

**We recommend that the Department submit federal fund reimbursement requests in a timely manner (repeat).**

## Procurement

### **Finding 2**

**The Department divided purchases of certain equipment maintenance services into multiple procurements and inflated the value of certain purchase orders.**

### **Analysis**

The Department divided purchases of certain equipment maintenance services into multiple procurements and inflated the value of certain purchase orders. According to State records, the Department processed purchase orders totaling \$3.9 million in calendar year 2018. We reviewed 12 purchase orders totaling \$577,000, each valued between \$45,000 and \$49,500, with effective dates between January 2018 and March 2019. Our review disclosed the following conditions:

- The Department artificially divided the purchase of hoist and crane equipment maintenance and repair services totaling \$294,000 into six procurements that were individually less than \$50,000. These procurements were not consolidated to maximize the State's purchasing power. In addition, this practice resulted in the circumvention of control agency approvals, such as by the Department of General Services (DGS), that would have been required for contracts over \$50,000.

When we inquired about these purchases, Department management disagreed with our characterization that this hoist and crane procurement was artificially divided and advised us that an individual procurement was conducted for each armory where the equipment was located. However, under State procurement regulations, this situation would not preclude the issuance of a request for proposals with a preference for the consolidation of these procurements. We believe that our position is justified by the fact that five of the six hoist and crane contracts were awarded to the same vendor.

- We found that the Department valued each of the 12 purchase orders we reviewed in amounts that exceeded the corresponding winning vendor bids. Specifically, the Department awarded the 12 purchase orders for a combined total of \$577,000 when the winning bids for the related contracts totaled approximately \$323,600. For example, for one purchase order totaling \$49,500, the winning bid on the contract totaled \$12,115. There was no documentation to justify the inflated purchase order values.

## **Recommendation 2**

**We recommend that the Department**

- a. discontinue the practice of dividing procurements and consolidate procurements of similar services to maximize purchasing power; and**
- b. discontinue the practice of inflating the purchase order values, and consult with DGS on what corrective action should be taken regarding the aforementioned inflated purchase orders.**

## **Payroll**

### **Finding 3**

**Supervisory reviews of adjustments to leave balances were not documented and were not performed by an independent employee.**

### **Analysis**

Supervisory reviews of adjustments to leave balances were not documented and were performed by an employee who also recorded related adjustments. During the three-year period ending May 20, 2019, 319 leave adjustments that increased employee leave balances by 8,176 hours were processed. For example, one adjustment increased an employee's sick leave balance by 621 hours (valued at approximately \$20,000) for time earned while the employee worked for another State agency. While a leave adjustment seemed appropriate under the circumstances, there was no documented review of this adjustment to ensure the amount of the adjusted leave was accurate and properly supported. During the same period, 387 leave adjustments that decreased employee leave balances by 10,007 hours were processed.

### **Recommendation 3**

**We recommend that the Department ensure that a documented review of leave adjustments is performed by an employee who does not have the capability to record those adjustments.**

**We advised the Department on accomplishing the necessary separation of duties using existing personnel.**

## **Audit Scope, Objectives, and Methodology**

We have conducted a fiscal compliance audit of the Military Department, for the period beginning July 1, 2015 and ending May 20, 2019. The audit was conducted 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.

As prescribed by the State Government Article, Section 2-1221 of the Annotated Code of Maryland, the objectives of this audit were to examine the Department's financial transactions, records, and internal control, and to evaluate its compliance with applicable State laws, rules, and regulations.

In planning and conducting our audit, we focused on the major financial-related areas of operations based on assessments of significance and risk. The areas addressed by the audit included federal fund reimbursements, cash receipts, payroll, procurements and disbursements, and equipment. We also determined the status of the findings contained in our preceding audit report.

Our audit did not include an evaluation of internal controls over compliance with federal laws and regulations for federal financial assistance programs and an assessment of the Department's compliance with those law and regulations because the State of Maryland engages an independent accounting firm to annually audit such programs administered by State agencies, including the Department.

To accomplish our audit objectives, our audit procedures included inquiries of appropriate personnel, inspections of documents and records, observations of the Department's operations, and tests of transactions. Generally, transactions were selected for testing based on auditor judgment, which primarily considers risk. Unless otherwise specifically indicated, neither statistical nor non-statistical audit sampling was used to select the transactions tested. Therefore, the results of the tests cannot be used to project those results to the entire population from which the test items were selected.

We also performed various data extracts of pertinent information from the State's Financial Management Information System (such as revenue and expenditure data) and the State's Central Payroll Bureau (payroll data) as well as from the contractor administering the State's Corporate Purchasing Card Program (credit

card activity). The extracts are performed as part of ongoing internal processes established by the Office of Legislative Audits and were subject to various tests to determine data reliability. We determined that the data extracted from these sources were sufficiently reliable for the purposes the data were used during this audit. Finally, we performed other auditing procedures that we considered necessary to achieve our audit objectives. The reliability of data used in this report for background or informational purposes was not assessed.

The Department's management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that objectives pertaining to the reliability of financial records; effectiveness and efficiency of operations, including safeguarding of assets; and compliance with applicable laws, rules, and regulations are achieved. As provided in *Government Auditing Standards*, there are five components of internal control: control environment, risk assessment, control activities, information and communication, and monitoring. Each of the five components, when significant to the audit objectives, and as applicable to the Department, were considered by us during the course of this audit.

Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate.

Our reports are designed to assist the Maryland General Assembly in exercising its legislative oversight function and to provide constructive recommendations for improving State operations. As a result, our reports generally do not address activities we reviewed that are functioning properly.

This report includes findings relating to conditions that we consider to be significant deficiencies in the design or operation of internal control that could adversely affect the Department's ability to maintain reliable financial records, operate effectively and efficiently, and/or comply with applicable laws, rules, and regulations. Our report also includes a finding regarding a significant instance of noncompliance with applicable laws, rules, or regulations. Other less significant findings were communicated to the Department that did not warrant inclusion in this report.

The Department's response to our findings and recommendations is included as an appendix to this report. As prescribed in the State Government Article, Section 2-1224 of the Annotated Code of Maryland, we will advise the Department regarding the results of our review of its response.

**APPENDIX**



LARRY HOGAN  
GOVERNOR  
COMMANDER-IN-CHIEF

STATE OF MARYLAND  
MILITARY DEPARTMENT  
FIFTH REGIMENT ARMORY  
BALTIMORE, MARYLAND 21201-2288

TIMOTHY E. GOWEN  
MAJOR GENERAL  
THE ADJUTANT GENERAL

May 10, 2019

Mr. Gregory A. Hook, CPA  
Legislative Auditor  
Office of Legislative Audits  
State Office Building, Room 1202  
301 West Preston Street  
Baltimore, Maryland 21201

Dear Mr. Hook:

Enclosed are the REVISED responses to the draft audit report from your Maryland Military Department fiscal activities for the period beginning July 1, 2015 and ending May 20, 2019.

If you have any questions, please contact Ms. Kelly Hammond at 410-234-3818 or email at [kelly.hammond2@maryland.gov](mailto:kelly.hammond2@maryland.gov).

Respectfully,

A handwritten signature in black ink, appearing to read "Timothy E. Gowen", with a large, sweeping flourish extending to the left.

Timothy E. Gowen  
Major General, MDARNG  
The Adjutant General

# Military Department

## Agency Response Form

### Federal Funds

**Finding 1**  
**The Military Department did not always submit requests for reimbursement of federal fund expenditures in a timely manner.**

**We recommend that the Department submit federal fund reimbursement requests in a timely manner (repeat).**

Agency Response			
<b>Analysis</b>			
<b>Please provide additional comments as deemed necessary.</b>	<p>Note #1: Due to lengthy periods of vacancy with the MEMA CFO position, certain grant reimbursement requests were submitted on untimely basis. Corrective action has been taken as described below.</p> <p>Note #2: During the audit period, a new federal processing tracking system was updated to help process NGB Cooperative Agreement reimbursements and the MMD Finance Office was able to consistently submit reimbursement requests within 30 days of month end closeout. However, in some instances lengthy delays occurred within the federal system to obtain necessary final approvals prior to the processing of the related reimbursement payment. Corrective action has been taken as described below.</p>		
<b>Recommendation 1</b>	Agree	<b>Estimated Completion Date:</b>	Completed
<b>Please provide details of corrective action or explain disagreement.</b>	<p><b>The Department has taken corrective action. Expenditures related to MEMA grants and NGB Cooperative Agreements are now being processed within a timely manner. Specifically, the MEMA Grants Office now meets with MEMA Finance Office on a quarterly basis to ensure that all federal grant drawdown requests are submitted within 90 days of expenditure. The MMD Finance Office will continue to submit cooperative agreement reimbursement requests into the federal processing system within 30 days of month end closeout. In addition, monthly meetings are now being held with federal representatives to ensure that reimbursement requests submitted into the federal system (along with any adjustments and final approvals) are processed timely (need to establish an acceptable standard).</b></p>		

# Military Department

## Agency Response Form

### Procurement

**Finding 2**  
**The Department divided purchases of certain equipment maintenance services into multiple procurements and inflated the value of certain purchase orders.**

We recommend that the Department

- a. **discontinue the practice of dividing procurements and consolidate procurements of similar services to maximize purchasing power; and**
- b. **discontinue the practice of inflating the purchase order values, and consult with DGS on what corrective action should be taken regarding the aforementioned inflated purchase orders.**

Agency Response			
Analysis			
<p><b>Please provide additional comments as deemed necessary.</b></p>	<p>Note #1: While the scope of this audit cannot include every agency contract or purchase order for the period of the audit, a review of MMD procurement practices would lead to the conclusion that MMD’s standard contracting practice has primarily been to contract for services by individual armory location, not bundle service contracts for armories by region, during the period of this audit and for prior years. MMD’s intent in this approach to contracting has never been to circumvent control agency approval, but to try to obtain bids for services where regionally bundled contracts would yield few bids, allow small businesses a better opportunity at state contracts and to obtain a lower cost for the state. MMD has consistently coordinated contracts that were anticipated to be over the small procurement threshold of \$50K with DGS. MMD notes that there are other state agencies who do not bundle service contracts for their individual facilities by region.</p> <p>Note #2: MMD has not sought to inflate the value of the referenced purchase orders, but has included both the preventive maintenance (PM) costs and an allowance amount for labor and parts for repairs performed in addition to PM into these purchase orders.</p>		
<p><b>Recommendation 2a</b></p>	<p>Agree</p>	<p><b>Estimated Completion Date:</b></p>	<p>Immediately</p>
<p><b>Please provide details of corrective action or explain disagreement.</b></p>	<p><b>MMD did not artificially divide or split procurements to avoid control agency (DGS) oversight. Maryland State’s Small Business Reserve (SBR) program allows small businesses to compete against other small businesses instead of larger, more established companies for contract awards. Agencies are required to spend at least 15% of their total fiscal year expenditures on qualified small business procurements. The crane and hoist contracts at individual armory</b></p>		

## Military Department

### Agency Response Form

	<p>locations were bid out that way in an attempt to allow smaller businesses the opportunity to bid. In previous crane and hoist contracts that were solicited by region, only one or two companies responded. MMD was seeking additional competition, which may have led to better pricing, and/or awards to small business on the new contracts. MMD did not foresee that five of the six contracts would be awarded to the same vendor. Again, the MMD intent was not to avoid DGS oversight, but to adhere to state guidelines for SBR goal. MMD will make sure that the SBR requirement is clearly indicated on future bid opportunities.</p>		
<b>Recommendation 2b</b>	Agree	<b>Estimated Completion Date:</b>	Immediately
Please provide details of corrective action or explain disagreement.	<p>The crane and hoists contracts had multiple pricing. BPOs were designed to cover the unknown repairs (labor had a fixed price) and parts (unknown price). MMD will immediately begin including detailed information regarding repairs on the purchase orders for this type of contract, specifically one line for the hourly labor rate, a second line with parts and a not to exceed price, and in the body of the PO a break down with guidelines for calculating payment based on historical data.</p>		

# Military Department

## Agency Response Form

### Payroll

**Finding 3**  
Supervisory reviews of adjustments to leave balances were not documented and were not performed by an independent employee.

We recommend that the Department ensure that a documented review of leave adjustments is performed by an employee who does not have the capability to record those adjustments.

We advised the Department on accomplishing the necessary separation of duties using existing personnel.

Agency Response			
<b>Analysis</b>			
<b>Please provide additional comments as deemed necessary.</b>	During the audit period, the employee (timekeeper approver) who performed the leave adjustment review was provided temporary authority to process leave adjustments after the retirement of the employee (timekeeper) responsible for making the leave adjustments.		
<b>Recommendation 3</b>	Agree	<b>Estimated Completion Date:</b>	Completed
<b>Please provide details of corrective action or explain disagreement.</b>	<b>Corrective action has been taken. The employee who performs the documented review of leave adjustments no longer has the capability to record those adjustments. The employee documents their review by signing the monthly leave adjustment report. After the vacant timekeeper position was filled and the new employee trained, that new employee began recording adjustments.</b>		

AUDIT TEAM

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