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Debra K. Davenport, CPA  
Auditor General  
State of Arizona Office of the Auditor General  
2910 North 44<sup>th</sup> Street, Suite 410  
Phoenix, Arizona 85018

Re: Performance Audit of the Arizona Department of Veterans' Services—Veterans' Donations  
and Military Family Relief Funds

Dear Ms. Davenport:

I have reviewed the Performance Audit of the Arizona Department of Veterans' Services—Veterans' Donations and Military Family Relief Funds. Please accept the following eleven (11) pages as the Department's response to the Audit. Enclosed are the Department's written comments on the report.

Sincerely,

Joey Strickland  
Director

**Recommendations:**

**1.1 Although existing statutes require the Department to comply with procurement and grant solicitation and award requirements regarding Veterans' Donations Fund expenditures, the Legislature should consider strengthening the existing statutory requirements to further clarify the Department's use of donations fund monies. The Legislature should consider the following two alternatives:**

- a. Modifying the donations fund statute in A.R.S. §41-608 to explicitly authorize the use of donations fund monies to provide grants to nonprofit organizations in compliance with grant solicitation and award statutes; or**
- b. Specifying that the Department should use donations fund monies itself to directly benefit veterans through its own programs, and thus prohibit the use of monies for grants to nonprofit organizations.**

**RECOMMENDATION 1.1**

**ADVS Response:** 1.1a and b. Although this recommendation is directed to the Legislature, the Department responds in part:

Our foremost goal *is* to benefit Arizona's veterans and their families.

In some cases, such as with a donation in April 2010, the Department, through the National Association of Drug Court Professionals, brought Erie County New York Judge Robert T. Russell to Phoenix for a meeting at the State Bar of Arizona in which Judge Russell shared his first-hand knowledge about how "Veterans' Courts" programs work in order to integrate and develop similar endeavors for Arizona veterans here in our state. Judge Russell is a recognized national expert on Veterans' Courts. By this "indirect" method, the Department's donation has led to the foundation in Maricopa County and in Tucson of Veterans' Courts which do directly benefit Arizona's veterans. The Department reasoned that the object sought, in this case the establishment of Veterans' Courts in Arizona, and the degree and manner in which that object affects the public welfare has indeed brought about a public benefit at least corresponds to the donation. This donation is one of the six (6) that the Auditor claims did not benefit Arizona veterans. (Page 8)

[\(See attached Auditor General Reply, Item #1a\)](#)

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Additionally, the suggestion in 1.1b that the Department use "donations fund monies itself to directly benefit veterans through its own programs" is precisely what the Department did in the instance cited by the Auditor General whereas the Department paid the Fiduciary Board investigation and disciplinary costs in 2009. Had this payment to the Court not been made, the possibility is great that the Court would have sanctioned further or even shut down the Veterans' Fiduciary program leaving our 252 qualifying number of clients without adequate representation.

[\(See attached Auditor General Reply, Item #1b\)](#)

Much of the "action" benefiting Arizona's veterans is conducted by nonprofit organizations such as the Veterans of Foreign Wars of the United States (VFW), the American Legion and their numerous Arizona posts as well as by locally created smaller nonprofit organizations throughout the state. Prohibiting the use of donation fund monies or grants to such nonprofit organizations would make it very difficult to provide needed assistance to veterans throughout the state especially in more remote areas where the only available assistance may be provided by such nonprofits.

"Nonprofit" does not mean the organization does not incur operational expense. In an ideal world, every dollar would go directly to the intended cause. The fact is that doesn't happen. Donations are divided between the organization's cause and operational costs involved in championing those causes. Charities with at least \$25,000.00 in gross receipts are required to report to the I.R.S. using the Form 990. It provides information on the filing organization's mission, programs, and finances. The Form 990 becomes the only public document that reports on the finances of charities.

According to the Center on Nonprofits and Philanthropy and the Urban Institute Center on Philanthropy of Indiana University, strict financial ratio standards between the percentage of donations spent for operational costs and the percent that goes directly to the "cause" favor larger organizations whose popular causes have been in existence for long periods. However, we have found that getting assistance out to Arizona veterans often involves using smaller nonprofit organizations that have direct access to the veterans in their locale.

Additionally, assisting some organizations with their fundraising creates a "multiplier effect" allowing those organizations to return a benefit to Arizona's veterans and public that far exceeds the consideration paid by the public fund.

The Department operates the donation fund in consultation with the Department's assigned assistant Attorney General. The Auditor General has recommended statutory changes be made and the department looks forward to working with the legislature.

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The conclusion that some expenditures may not have benefited Arizona veterans is the opinion of the auditor and differs from that of the Department. The public, Arizona veterans and dependents in particular, received a value much greater than the Department expenditure through such assistance to military veterans and their families for rent and mortgage assistance, food, vehicle payments, vehicle repair, emergency financial assistance, in-state tuition at state colleges and universities for all veterans and spouses with an honorable discharge, veteran supportive campuses, veteran employment training, and two veteran diversion courts (Tucson and Phoenix). The auditor general's assertion fails in each case to show that the accomplishments sought and the manner in which each affected Arizona Veterans and families did not serve a public purpose.

(See attached Auditor General Reply, Item 1)

Neither the donation fund statute, A.R.S. §41-608 nor the Auditor General's November 2009 report

([http://www.auditorgen.state.az.us/Reports/State\\_Agencies/Agencies/Veterans\\_Services\\_Department\\_of/Veterans\\_Services\\_Department\\_of.htm](http://www.auditorgen.state.az.us/Reports/State_Agencies/Agencies/Veterans_Services_Department_of/Veterans_Services_Department_of.htm))

specifically cites A.R.S. §41-2701 et seq (the grant solicitation and award statues) as a statute that should have been followed in regard to the donation fund. Nor have our repeated consultations with the Attorney General's office on how best to use the donation fund resulted in the Department being advised that it must follow A.R.S. §41-2701 et seq in connection with the donation fund.

Nor does a search of various statutorily created funds from A. R. S. 15-243, the Golden Rule Special Plate Fund, to A. R. S. 28-2435, the Arizona Masonic Fraternity Special Plates Fund, find any that specifically references that A.R.S. §41-2701 et seq must be followed in determining the recipient(s) of funds raised by the sale of those plates. In fact, and as an example, A.R.S. 28-2435 requires the trustees of the donating entity to distribute the monies in the fund to charities supported by Arizona Masons.

We welcome the opportunity to work with the members of the Arizona Legislature to further clarify the mechanics of using the donation fund.

**RECOMMENDATION:**

**1.2 To better ensure that Veterans' Donation Fund monies are used appropriately, the Legislature should also consider revising statute to add more restrictive requirements to the donations fund. These additions include:**

- a. Eliminating the language that states that expenditures are to be made "at the discretion of the director,"
- b. Specifying what fund monies may and may not be used for;
- c. Requiring that the Arizona veterans' Service Advisory Commission or some other external body review and approve expenditures from the donations fund; and
- d. Requiring an annual reporting requirement by the Director to the Arizona Veterans' Service Advisory Commission, the Governor, or another external body that includes a detailed listing of expenditures from the fund.

**RECOMMENDATION 1.2**

**ADVS Response:** Since this recommendation is to the Legislature, the Department has no response. We welcome the opportunity to work with the members of the Arizona Legislature to further clarify the mechanics of using the donation fund.

**RECOMMENDATION:**

**1.3 Unless the Legislature amends statute to require it to spend Veterans' Donations Fund monies directly instead of giving it to other organizations, the Department should develop and implement a formal grant process and develop policies and procedures that comply with A.R.S. §§41-2701 through 41-2706 that govern grant solicitation and award. The process should be followed for all donations fund expenditures except for purchases of goods and services and should encompass all statutory requirements for grant solicitation and award, including:**

**a. Issuing a request for grant applications that includes:**

- A description of the nature of the grant project, including the funding source and total amount of available monies;**
- The criteria or factors under which applications will be evaluated and the relative importance of each criteria or factor; and**
- The due date for submittal of applications and the anticipated time the awards may be made.**

**b. Public notice of the request for grant applications at least 6 weeks before the application due date, and public receipt of grant applications at the time and place designated in the request.**

**c. Review of the applications by at least three evaluators, based solely on the evaluation criteria or factors set forth in the request for grant applications, and a written record of the assessment of each application; and**

**d. Evaluators' recommendations to the Director, who may affirm, modify, or reject the recommendations and a written record of the justification for the Director's actions if he/she does not affirm the evaluators' recommendations.**

### **RECOMMENDATION 1.3**

**ADVS Response:** The finding of the Auditor General is not agreed to, but the recommendation will be implemented.

The Department will work with members of the Arizona Legislature in assisting to determine the best method of revising its administration of the VDF. The Department anticipates there will be further guidance given by way of a statutory change and once received it is the Department's intention to follow that guidance along with complying with all applicable statutes.

### **RECOMMENDATION:**

**1.4 To help ensure that Veterans' Donations Fund monies are spent appropriately, the Department should:**

- a. Require recipients to provide a report on how money provided from the donations fund was actually used, including providing supporting documentation such as receipts and invoices, and communicate to applicants that misuse of monies or failure to provide this information will cause any future requests to be denied, and**
- b. Require applicants for donations fund monies to sign the application or donations fund request form that provides a sworn statement certifying that the funds will be used for the requested purpose.**

### **RECOMMENDATION 1.4**

**ADVS Response:** The finding of the Auditor General is agreed to and a different method of dealing with the finding will be implemented. We welcome the opportunity to work with the members of the Arizona Legislature to further clarify the mechanics of using the donation fund. The Department plans to modify the donation fund request form to include a requestor signature block. The Department will also continue to request summations from the applicants as to their successes, and accomplishments. Additionally, as the Auditor General has recommended, following any statutory changes the Department will comply with the applicable state statutes.

**RECOMMENDATION:**

**1.5 Consistent with the recommendations in the 2009 report, the Department should:**

- a. **Limit Veterans' Donations Fund expenditures to only those requests that benefit Arizona veterans; and**
- b. **Seek and document legal advice prior to making expenditures of \$5,000 or more to ensure the Department's compliance with applicable state laws, regulations, and executive orders; and**

**RECOMMENDATION 1.5a**

**ADVS Response:** The finding of the Auditor General is agreed to and the recommendation will not be implemented. The Department maintains that expenditures made from the Veterans' Donation Fund have benefited Arizona veterans.

**RECOMMENDATION 1.5b**

**ADVS Response:** The finding of the Auditor General is not agreed to and the recommendation will not be implemented.

The Department has sought legal advice on many issues including use of the donation fund. The Department is engaged in legal discussions with the assigned assistant AG at our regular staff meetings and special meetings as necessary. Counsel is an intricate part of the Department and remains well versed on the Department's use of the donation fund as well as many other areas of the Department's operation.

The Department strives to follow all state procedures and codes as applicable.

**RECOMMENDATION:**

- 2.1 The Committee should establish additional award criteria to prevent inconsistent recommendations, but allow for exceptions upon written explanation of reasoning. These criteria should specify:**
- a. Factors that will be considered during the decision-making process;**
  - b. Expenses that are and are not eligible for award; and**
  - c. Documentation applicants should submit to support financial assistance requested in the application.**

**Committee response:**

The finding of the Auditor General is not agreed to, but the recommendation will be implemented. Basic award criteria were established in the governing statute and further refined in the Committee's Guidelines and Bylaws for the Arizona Military Family Relief Fund (MFRF) Advisory Committee (current revision Aug 2010). We have reviewed the extensive guidance of six other states and the AZ National Guard. A number of applications received by the AZ MFRF have been the result of restrictive criteria established by the AZ NG fund, precluding a number of applicants from receiving assistance and turning to the AZ MFRF instead. Additionally, after reviewing the guidance used in a number of other states, applicants must sort through lengthy, complicated requirements to even determine if they are eligible to apply. Having dealt with a large number of applicants at the AZ MFRF, it is clear the process and criteria must be simple for applicants dealing with stress, grief or tragedy to easily make their own determination whether to apply for assistance.

The Auditor General's Report cites a number of instances where the MFRF Committee's simple set of criteria led to inconsistent awards. In fact, the awarded grants under the AZ MFRF have been generally consistent; the complete record of rationale used in the cases cited is missing. This shortfall in the process has been corrected and records of decisions along with specific rationale are now recorded. In some cases, the Auditor cited lack of documentation or missing documentation. Every case is unique in its own right and verification of service, residency, wartime deployment, VA disability and other documentation is often not available in written form. In those cases the Committee verbally verified information via phone calls with the assigned service liaisons for injured service members, the VA, Veterans Service Organization representative, creditors and other sources through our ADVS representative. In not all cases were those conversations documented with a memo; that has been corrected. The AZ MFRF

Committee always seeks improvement in our volunteer operation and consequently, the Committee will review the comparable processes of the states of Maine, California, Missouri, Louisiana, Illinois and Michigan and our own experience and revise its Guidelines to include more specific factors in the decision-making process. We will also consider adding more specific expenses that will/will not be covered and how they will be paid (direct to creditors, not individuals). Required documents to be provided by the applicants are already listed on the application form; however, we will review the form to ensure clarity in the forms needed for the decision-making process.

**RECOMMENDATION:**

**2.2 The Committee should document the reasons for its recommendations, including how the recommendations are based on the established criteria, and provide these reasons to the Director as part of its recommendations for approving, partially approving, or denying applications.**

**Committee Response:**

The finding of the Auditor General is agreed to and the audit recommendation will be implemented. Effective during the 23 June 2011 MFRF meeting, each motion made by a member of the Committee towards an award decision included the rationale for approving, partially approving or disapproving an application. In the event the rationale is inadvertently not provided, the AZDVS representative supporting the board queries the Committee member making the motion for specific rationale for the motion as it relates to the award criteria. Further, the AZDVS representative includes the rationale information along with the Committee's decision to the Director for review.

**RECOMMENDATION:**

**2.3 The Department should develop and implement a process to inform applicants in writing of the reasons for the decisions regarding their applications.**

**ADVS Response:**

The finding of the Auditor General is agreed to and the audit recommendation will be implemented. Effective 23 June 2011, each applicant now receives a letter in addition to verbal notification to inform them of the decision on their application and the rationale, their right to appeal and the appeals process.

**RECOMMENDATION:**

**2.4 The Department should improve its appeals process by:**

- a. **Modifying the proposed rules to conform with A.R.S. §41-2704 and clearly explain the process; and**
- b. **Developing and implementing a process for informing applicants in writing that they have this option.**

**ADVS Response:**

The finding of the Auditor General is agreed to and the audit recommendation will be implemented. The proposed rules for the Arizona Military Family Relief Fund will be modified to conform to A.R.S. §41-2704, and the revised appeals process has been put into practice. The Deputy Director will either approve or deny an application after receiving the Advisory Committee's recommendation. If the Deputy Director denies an application, the applicant may then appeal the decision to the Director who has not played any previous role in the decision making process. Applicants can then appeal a decision by the Director to the Director of the Department of Administration. Applicants are informed of their right to appeal and the appeals process in the written notification they receive informing them of the decision regarding their application and the reasoning.

**RECOMMENDATION:**

**2.5 To comply with A.R.S. §41-2705 and avoid real or perceived bias in committee recommendations:**

- a. **The Department should develop a statement for committee members to sign prior to considering applications, indicating that they have no undisclosed interest in the decision and no undisclosed contact with applicants while the application is under consideration; and**
- b. **The Committee should consider adopting a practice of discussing any relationships with applicants at each meeting and reminding members that they can recuse themselves from decisions when appropriate.**

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**ADVS Response:**

The finding of the Auditor General is agreed to and the audit recommendation will be implemented. The Department will work with our Assistant Attorney General to develop such a statement and have all Committee members sign this statement. The Committee already practices disclosing any information regarding a relationship a committee member may have with an applicant, whether that relationship is professional or personal, and each committee member understands the necessity of recusing oneself when appropriate. In July 2011, the Committee chairman directed a standard item be added to all meeting agendas where the Chairman will remind Committee members to disclose knowledge of applicants and recuse themselves in decision making if that knowledge or relationship could constitute undue bias. These current practices will be included in the disclosure statement created for the committee members to sign.

**RECOMMENDATION:**

- 2.6 The Department should request that its assistant attorney general regularly attend committee meetings to help ensure compliance with statutory requirements.**

**ADVS Response:**

The finding of the Auditor General is agreed to and the audit recommendation will be implemented. The Department's Assistant Attorney General has been informed of all Advisory Committee meetings and invited to attend. This practice will continue, but attendance is ultimately determined by the Assistant Attorney General's schedule and availability. Due to recent reductions in the staffing in the Office of the Attorney General, we have been informed they have been unable to support our meetings.

# AUDITOR GENERAL REPLY TO AGENCY RESPONSE

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The following comments are provided to address certain statements the Department of Veterans' Services (Department) made related to Finding 1, Recommendation 1.1, regarding the Veterans' Donations Fund (donations fund):

1. The Department states that the Auditor General's conclusion that some expenditures did not benefit Arizona veterans is the opinion of the Auditor General and that the Auditor General did not show that the expenditures did not benefit Arizona veterans or serve a public purpose. The Auditor General's findings and conclusions are based on a review of available department documentation and applicable Arizona laws and regulations, not opinion. The responsibility rests with the Department, not the Auditor General, to show whether donations fund expenditures benefited Arizona veterans and served a public purpose. The Auditor General disagrees that all donations fund expenditures reviewed by auditors either directly or indirectly benefited Arizona veterans. For example:
  - a. The Department asserts that its expenditure of \$10,000 to a national nonprofit organization indirectly benefited Arizona veterans because it helped to establish two veterans' drug treatment courts in Arizona (see page 1 of the Department's response). According to the Department, these monies were used to bring a national expert to the State for this purpose. However, as noted on page 8 of the report, the funding request stated that the monies would be used to support new and existing veterans' drug treatment courts nation-wide and to help other states develop legislation to support this program. In addition to these discrepancies, the Department lacks documentation to show how the \$10,000 was actually spent.
  - b. The Auditor General disagrees that the Department's expenditure of donations fund monies to pay investigation and disciplinary proceeding costs to the Arizona Supreme Court benefited Arizona veterans (see page 2 of the Department's response). As noted on page 8 of the report, these costs resulted directly from the Department's mismanagement of its fiduciary program and failure to fulfill its fiduciary responsibility to its clients—Arizona veterans. Thus, the Department asserts that its spending of donations fund monies benefited Arizona veterans because it failed to benefit Arizona veterans through its fiduciary program.