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OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

FINANCIAL AUDIT DIVISION REPORT

Department of Human Services

Federal Compliance Audit

Year Ended June 30, 2008

March 26, 2009 **Report 09-10**

FINANCIAL AUDIT DIVISION
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OFFICE OF THE LEGISLATIVE AUDITOR

State of Minnesota • James Nobles, Legislative Auditor

March 26, 2009

Senator Ann H. Rest, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. Cal R. Ludeman, Commissioner
Department of Human Services

This report presents the results of our audit of certain federal financial assistance programs administered by the Department of Human Services during fiscal year 2008. We conducted this audit as part of our audit of the state's compliance with federal program requirements. We emphasize that this has not been a comprehensive audit of the Department of Human Services.

We discussed the results of the audit with department staff at an exit conference on March 13, 2009. This audit was conducted by Michael Hassing, CPA, CISA (Audit Manager), Susan Kachelmeyer, CPA, CISA (Auditor-in-Charge), Sonya Johnson, CPA (Director of Investigations), and Melanie Greufe (Lead Worker). They were assisted by the following auditors: Sara Becker; Kayla Borneman, CPA; Jerry Foty; Chau Nguyen; Paul Thompson; Emily Wiant; Zach Yzermans, CPA; and Mai Na Yang.

This report is intended for the information and use of the Legislative Audit Commission and the management of the Department of Human Services. This restriction is not intended to limit the distribution of this report, which was released as a public document on March 26, 2009.

We received the full cooperation of department staff while performing this audit.

/s/ James R. Nobles	*/s/ Cecile M. Ferkul*
James R. Nobles Legislative Auditor	Cecile M. Ferkul, CPA, CISA Deputy Legislative Auditor

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Report Summary

Conclusion

The Minnesota Department of Human Services generally complied with and had controls to ensure compliance with provisions of laws, regulations, contracts, and grants applicable to the federal programs we audited for fiscal year 2008. However, the department had some significant control deficiencies, as described in findings 2 to 10 in this report. We consider the deficiencies in findings 2 and 3 to be material weaknesses.

Key Findings

- The Department of Human Services did not identify, analyze, and document their internal controls over compliance with federal single audit requirements. (Finding 1, page 7)
- The Department of Human Services lacked controls over certain financial processes to prevent or detect Medical Assistance (CFDA 93.778) payments to a fraudulent vendor. (Finding 2, page 8)
- The Department of Human Services did not adequately advise counties about federal compliance and audit requirements. (Finding 3, page 8)
- The Department of Human Services did not adequately protect not public data on individuals. (Finding 4, page 9)
- The Department of Human Services provided federal reimbursements for ineligible adoption assistance services (CFDA 93.659). (Finding 10, page 14)

Audit Scope

Programs material to the State of Minnesota's federal program compliance for fiscal year 2008 at the Department of Human Services.

Selected Audit Areas:

- Food Stamp Cluster
  - Food Stamps and Food Stamp Administration (CFDA 10.551/10.561)
- Temporary Assistance for Needy Families (CFDA 93.558)
- Child Support Enforcement (CFDA 93.563)
- Child Care Cluster
  - Child Care and Development Block Grant (CFDA 93.575)
  - Child Care Mandatory and Matching Fund (CFDA 93.596)
- Foster Care (CFDA 93.658)
- Adoption Assistance (CFDA 93.659)
- Social Services Block Grant (CFDA 93.667)
- State Children's Health Insurance Program (CFDA 93.767)
- Medicaid Cluster
  - State Medicaid Fraud Control Unit (CFDA 93.775)
  - Hurricane Katrina Relief (CFDA 93.776)
  - State Health Care Providers Survey (CFDA 93.777)
  - Medical Assistance Program (CFDA 93.778)
- Substance Abuse Prevention and Treatment Block Grant (CFDA 93.959)

Department of Human Services

Federal Program Overview

The Department of Human Services administered federal programs that we considered major federal programs for the State of Minnesota, subject to audit under the federal Single Audit Act.[1] Table 1 identifies these major federal programs.

Table 1
Major Federal Programs
Administered by the Department of Human Services
Fiscal Year 2008

CFDA[1]	Program Name	Expenditures
	Food Stamp Cluster[2]	
10.551	Food Stamps	$322,454,717
10.561	Food Stamps Administration	$53,659,667
93.558	Temporary Assistance for Needy Families	$223,829,319
93.563	Child Support Enforcement	$93,752,485
	Child Care Cluster	
93.575	Child Care and Development Block Grant	$55,578,550
93.596	Child Care Mandatory and Matching Fund	$57,913,027
93.658	Foster Care	$51,614,057
93.659	Adoption Assistance	$23,970,215
93.667	Social Services Block Grant	$33,852,098
93.767	State Children's Health Insurance Program	$72,235,296
	Medicaid Cluster	
93.775	State Medicaid Fraud Control Unit[3]	$904,743
93.776	Hurricane Katrina Relief	$7,965
93.777	State Health Care Providers Survey	$4,346,942
93.778	Medical Assistance Program	$3,517,772,457
93.959	Substance Abuse Prevention and Treatment Block Grant	$22,979,128

[1]The Catalog of Federal Domestic Assistance (CFDA) is a unique number assigned by the federal government to identify its programs.

[2]A cluster of programs is a group of closely related programs that have similar compliance requirements and are treated as a single program.

[3]The State Medicaid Fraud Control Unit is administered through the Minnesota Office of the Attorney General. We performed specific federal compliance audit work on this program for fiscal year 2008. We did not report any written findings or recommendations.

Source: Minnesota Accounting and Procurement System.

[1] We defined a major federal program for the State of Minnesota in accordance with a formula prescribed by the federal Office of Management and Budget as a program or cluster of programs whose expenditures for fiscal year 2008 exceeded $23.8 million.

Objective, Scope, and Methodology

The objective of our audit was to determine whether the Department of Human Services complied with federal program requirements in its administration of these federal programs for fiscal year 2008. This audit is part of our broader federal single audit objective to obtain reasonable assurance about whether the State of Minnesota complied with the types of compliance requirements that are applicable to each of its federal programs.[2] In addition to specific program requirements, we examined the department's general compliance requirements related to federal assistance, including its cash management practices.

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 the *Government Auditing Standards*, issued by the Comptroller General of the United States of America and with the U.S. Office of Management and Budget's *Circular A-133 Compliance Supplement.*

Conclusions

The Department of Human Services generally complied with and had controls to ensure compliance with certain provisions of laws, regulations, contracts, and grants applicable to its major federal programs for fiscal year 2008. However, the department had some significant control deficiencies, described in findings 1 through 10 in the following *Findings and Recommendations* section. We consider the deficiencies described in findings 2 and 3 to be material weaknesses. A material weakness is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material noncompliance with federal regulations will not be prevented or detected by the department's internal control.

[2] The State of Minnesota's single audit is an entity audit of the state that includes both the financial statements and the expenditures of federal awards by all state agencies. We issued an unqualified audit opinion, dated December 9, 2008, on the State of Minnesota's basic financial statements for the year ended June 30, 2008. In accordance with *Government Auditing Standards*, we also issued our report, dated December 9, 2008, on our consideration of the State of Minnesota's internal control over financial reporting and our tests of compliance with certain provisions of laws, regulations, contracts, and grants. (Office of the Legislative Auditor's Financial Audit Division Report 09-03, *Report on Internal Control Over Financial Reporting*, issued February 13, 2009.) This report included control deficiencies related to the Department of Human Services.

We have reported these weaknesses to the federal government in the *Minnesota Financial and Compliance Report on Federally Assisted Programs*, prepared by the Department of Finance.[3] This report provides the federal government with information about the state's use of federal funds and its compliance with federal program requirements. The report includes the results of our audit work, conclusions on the state's internal controls over and compliance with federal programs, and findings about control and compliance weaknesses.

[3] Effective June 2008, the Legislature reorganized the Department of Finance to include the duties of the Department of Employee Relations. Although still identified in statute as the Department of Finance, in October 2008, the department changed its name to Minnesota Management and Budget. The department will seek legislative approval for the name change in the 2009 legislative session.

Findings and Recommendations

Finding 1

The Department of Human Services did not identify, analyze, and document its internal controls related to business operations and the schedules of federal expenditures.

The department did not have a comprehensive risk assessment pertaining to its internal controls over compliance with federal single audit requirements.[4] The department has an increased likelihood of a control deficiency if it does not clearly communicate to all staff its risks, control activities, and monitoring policies and procedures.

State policy details that each agency head has the responsibility to identify, analyze, and manage business risks that affect an entity's ability to maintain its financial strength and the overall quality of its products and government services.[5] This policy also requires communication of the internal control policies and procedures to all staff so they understand expectations and the scope of their freedom to act. This policy also requires follow-up procedures that, at a minimum, should include mechanisms for monitoring results and reporting significant control deficiencies to individuals responsible for the process or activity involved, including the agency's executive management and other individuals in a position to take corrective action. A new audit standard[6] reinforced management's responsibility to have effective internal controls over its financial operations. The federal government expects that those controls also ensure compliance with federal program requirements.

The Department of Human Services is aware of certain risks, has many control activities in place, and performs selected internal control monitoring functions. In addition, it has begun a process of identifying and documenting risks and related control activities. However, the department has not identified and analyzed all the risks, designed comprehensive controls to address significant risks, or developed sufficient monitoring procedures to ensure that controls are in place and are effective to reduce the significant risks identified.

Findings 2 through 10 identify deficiencies in the department's internal control procedures and specific noncompliance with federal requirements that the department's internal control structure did not prevent or detect. If the department had a comprehensive internal control structure, it should have identified these deficiencies, assessed the degree of risk of these deficiencies,

[4] This control deficiency is related all major federal programs identified in Table 1.
[5] Department of Finance Policy 0102-01.
[6] Statement on Auditing Standards #109.

designed control procedures to address significant risks, and monitored whether controls were working as designed and effective in reducing the risks to an acceptably low level. It is likely that the department will continue to have noncompliance and weaknesses in internal controls over compliance until it operates within a comprehensive internal control structure.

Recommendation

- *The Department of Human Services should continue to review and clearly document its risks, control activities, and internal control monitoring functions for its key business processes.*

Finding 2

The Department of Human Services lacked controls over certain financial processes to prevent or detect payments to a fraudulent vendor.

The department had poor controls over several key areas that allowed an employee to make payments to a fraudulent vendor. Appendix A contains our letter identifying the control deficiencies that allowed the fraud to occur.

The employee initiated 23 medical assistance payments to a fraudulent vendor between August 2003 and September 2008 totaling $1.1 million, of which $353,000 was from the Medical Assistance Program (CFDA 93.778).

Recommendation

- *The department should strengthen its internal controls over the payment process to ensure:*
  - *adequate separation of incompatible duties, including limitations of system access to employees' specific job responsibilities; and*
  - *valid payments to legitimate vendors.*

Finding 3

The Department of Human Services did not adequately advise counties about federal compliance and audit requirements.

For some federal programs, including the Medical Assistance Program (CFDA 93.778), the Department of Human Services did not appropriately notify counties that they were subrecipients of federal funds or identify the compliance requirements related to those funds, including the need for audit coverage under the Single Audit Act.[7] As a result, counties did not identify the expenditures of these funds as federal grant expenditures, and their auditors did not include these

[7] Office of Management and Budget Circular A-133, Subpart D.400(d).

expenditures in the scope of the counties' single audits. We estimate that counties omitted at least $100 million of federal program expenditures from their single audit coverage.

In addition, the department's subrecipient monitoring process did not identify that the scope of counties' single audits did not include significant amounts of federal pass-through grants.

Upon learning of this deficiency in February 2009, the department revised and reissued instructional bulletins to the counties to help them accurately record and identify these pass-through federal grants. This should result in the inclusion of these expenditures in subrecipient single audits for calendar year 2008, which are part of the State of Minnesota's 2009 single audit reporting package.

Recommendations

- *The Department of Human Services should properly classify and monitor all of its federal awards to other governmental entities to ensure that subrecipients are aware of program compliance requirements, accurately account for all subgranted federal funds and include those funds in the scope of their annual single audits.*
- *The Department of Human Services needs to notify the federal Department of Health and Human Services about this significant weakness in its administration of federal funds and determine whether it needs to take additional actions to resolve this issue and if there are any sanctions to the state.*

Finding 4

The Department of Human Services did not adequately protect not public data on individuals.

The department did not sufficiently protect not public data on individuals. It sometimes recorded assistance recipients' names and social security numbers in the vendor invoice field on the state's accounting system. While this allowed the service providers receiving the payment to identify the client that the payment was for, it also allowed anyone with access to this table in the state's information warehouse to obtain this not public data. State statutes define data on individuals that is collected, maintained, used, or disseminated by a welfare system as private data on individuals.[8] The statutes prohibit the Department of Human Services and other departments with public assistance systems from disclosing the data except under very restricted circumstances. In addition, state policy categorizes

[8] *Minnesota Statutes* 2008, Chapter 13.

accounting system data as public and specifically instructs state agencies that names and health-related information on individuals should not be included.[9]

Recommendation

- *The Department of Human Services should eliminate not public data from the accounting system or work with the Department of Finance to restrict access to the data.*

Finding 5

Prior Finding Partially Resolved: The Department of Human Services did not validate its federal program payroll costs.

The department did not comply with some requirements for payroll it charged to federal programs. Federal regulations require that employees who work on a single federal program support their payroll charges by certifying at least every six months that they worked solely on that program for the period covered by the certification.[10] Employees who work on multiple federal programs need to support charges for these salaries and wages with signed, after-the-fact activity reports that account for the employees' total compensated activities at least monthly.[11]

The department did not always comply with these requirements for payroll it charged to federal programs, as explained below:

- The department did not conduct quarterly time studies for two of four employees we tested that were paid from multiple federal programs, including the Temporary Assistance to Needy Families Program (CFDA 93.558). The department inappropriately used certifications to support these payroll charges.

- Some certifications and activity reports were not properly authorized. Signatures provide a validation of the hours charged to federal programs. The department had the following weaknesses:
  - Two employees, paid in part from the Temporary Assistance to Needy Families Program (CFDA 93.558), did not sign their activity reports and were not submitting reports on a monthly basis.
  - Some employees who charged time to the Substance Abuse Program (CFDA 93.959) did not have properly authorized activity reports. Four activity reports were not signed by the employees; one

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[9] Department of Finance Policy 0803-01.

[10] U.S. Office of Management and Budget Circular A-87, *Cost Principles for State, Local, and Indian Tribal Governments.*

[11] U.S. Office of Management and Budget Circular A-87, *Cost Principles for State, Local, and Indian Tribal Governments.*

certification was signed by a supervisor who did not oversee the employee's work; and one certification was signed by the employee as the supervisor.

- o The department did not have documentation to support the authorization of activity reports for some employees working in the Foster Care (CFDA 93.658) and Adoption Assistance (CFDA 93.659) programs. The department established an email authorization process, but deleted the emails validating the hours worked on these programs.

Although these weaknesses existed, the department made some progress in implementing recommendations noted in our prior audit report.[12] The department improved its centralized controls over the certification process for federally funded payroll costs.

Recommendation

- *The Department of Human Services should continue to review and monitor its federal payroll verification processes to reduce the potential for inaccurate federal payroll certifications and unauthorized activity reports.*

Finding 6

Prior Finding Not Resolved: The Department of Human Services submitted reports to the federal government late for three federal programs.

The department did not maintain sufficient internal controls to ensure the timeliness of reports for three of its federal programs - the Medical Assistance Program (CFDA 93.778), the State Children's Health Insurance Program (CFDA 93.767), and the State Health Care Providers Survey (CFDA 93.777). The department has been unable to meet the 30-day reporting requirement for filing quarterly reports to the federal government for several years. During fiscal year 2008, the department electronically filed the reports from 30 to 95 days after the due date. The federal government relies on the reports to ensure that program objectives are being met and that the state is appropriately managing and monitoring the federal award.

Recommendation

- *The Department of Human Services should improve its reporting process to ensure timely completion of all of its federal reports.*

[12] Office of the Legislative Auditor's Financial Audit Division Report 08-12, *Department of Human Services*, issued March 28, 2008.

Finding 7

The Department of Human Services did not properly record the liability date for nearly $1.3 million of Child Support Enforcement Program's expenditure transactions in the state's accounting system.

The department did not record the correct date the state incurred a liability for three items tested within the Child Support Enforcement Program (CFDA 93.563). For these transactions, the state incurred a liability in fiscal year 2008, but coded the activity to fiscal year 2009 in the state's accounting system. The three expenditures, recorded in July and August 2008, totaled $1,269,667. According to state policy,[13] agencies must accurately enter the date that goods are received or services provided to ensure proper recognition of the transaction for financial reporting. This is particularly important during the annual close period from July 1 through the end of August when two budget fiscal years are open. In this case, we adjusted the program's Schedule of Expenditures of Federal Awards for fiscal year 2008 by the $1,269,667 accrual error.

Recommendation

- *The Department of Human Services should have a process to record and review the correct liability date in the state's accounting system to ensure accurate financial reporting.*

Finding 8

Prior Finding Not Resolved: The Department of Human Services was not in compliance with federal cash management requirements.

The department did not comply with its Treasury-State Agreement for the Temporary Assistance for Needy Families Program (CFDA 93.558) and the Child Care Cluster Program (CFDA 93.575 and 93.596). In accordance with the federal Cash Management Improvement Act, the department agreed to minimize the time it holds federal cash. For both these programs, the department agreed to a one-day clearing pattern between draws and expenditures of federal funds.

For the Temporary Assistance for Needy Families Program, the department exceeded its one-day limit and had significant excess cash on hand for five occurrences throughout fiscal year 2008. The number of consecutive days in which the program had positive cash balances ranged from 2 to 8 days for a total of 22 days, and the positive federal cash amounts per day were from $6,500 through $6,800,000. The average daily balance during those periods was approximately $3 million.

For the child care cluster programs, the department exceeded its one-day limit and had excess cash on hand for nine occurrences throughout fiscal year 2008. The

[13] Department of Finance Policy 0901-01.

number of consecutive days in which this program had positive cash balances ranged from 2 to 9 days for a total of 38 days, and the positive federal cash amounts per day were from $31,000 through $9,500,000. The average daily balance during those periods was approximately $2 million.

The Substance Abuse Prevention and Treatment Program (CFDA 93.959), which is not included in the Treasury-State Agreement, also did not minimize the time it held federal cash. The Substance Abuse Program's cash balance was positive every day of fiscal year 2008. About half of the daily balances were less than $12,000, while the other balances ranged as high as $1,800,000. The average daily balance during fiscal year 2008 was approximately $135,000.

Recommendation

- *The Department of Human Services should comply with the federal Cash Management Improvement Act and its Treasury-State Agreement by better monitoring and maintaining minimum program cash balances.*

Finding 9

The Department of Human Services did not comply with federal suspension and debarment requirements.

The Department of Human Services did not verify the suspension and debarment status of vendors with whom it entered into annual plan agreements. The department used annual plan agreements to contract for professional/technical services costing less than $5,000. Federal requirements prohibit state agencies from contracting with vendors listed as suspended or debarred.[7] For these annual plan vendors, the department did not have the vendor certify as part of the annual plan agreement that it was not suspended or debarred. The department could not show that it had verified that the vendor was not on the federal excluded parties list of suspended or debarred vendors. However, our audit testing did not identify any suspended or debarred vendors.

Recommendation

- *The Department of Human Services needs to ensure compliance with federal requirements by verifying suspension and debarment for all federally funded contracts or having vendors certify they are not suspended or debarred.*

[7] U.S. Office of Management and Budget Circular A-133, Part 3 – Compliance Requirements.

Finding 10

The Department of Human Services provided federal reimbursements for ineligible adoption assistance services.

The Department of Human Services paid $5,500 in federal reimbursements under the Adoption Assistance Program (CFDA 93.659) for unallowable costs. The department made payments to an adoption assistance agency for three clients that did not meet the federal program eligibility requirements. The department made payments to the vendor even though the department's documentation indicated the clients were not eligible for these services. The department did not have an effective internal control process to detect errors or review the payment documentation. There is an increased risk for fraud under the current process.

Recommendations

- *The Department of Human Services needs to review its Adoption Assistance Program*'s *eligibility and payment processes to ensure that it does not make payments for ineligible clients.*
- *The department needs to recover the questioned costs for the unallowable expenditures.*
- *The department should review other payments made to this vendor and to other vendors within this program to ensure that it did not incur other unallowable costs.*

Appendix A

Communication to Legislators Concerning Fraud at the Minnesota Department of Human Services

Date: February 6, 2009

To: Members of the Legislative Audit Commission
Members of House and Senate Health and Human Services Committees
Members of House and Senate State Government Finance Committees

From: James Nobles, Legislative Auditor
Cecile Ferkul, Deputy Legislative Auditor

Subject: Fraud at the Minnesota Department of Human Services

On January 15, 2009, Kim Austen, a former employee of the Minnesota Department of Human Services, pleaded guilty to using her position to steal more than $1 million from the state's Medical Assistance program. While federal authorities took charge of investigating and prosecuting the case, the Office of the Legislative Auditor (OLA) reviewed the fraud from a state perspective. The purpose of this letter is to convey our findings to the Legislative Audit Commission and other interested legislators.

Ms. Austen was hired by the Department of Human Services in 1981, and had worked as a supervisor in the department's medical payments support unit since 1997. She was a trusted employee who had an in-depth understanding of the department's payment systems. Other employees and officials often came to her for advice in helping to resolve questions and problems related to medical payments and vendors. Ms. Austen used her expertise, experience, and authority to perpetrate the fraud.

Because federal authorities preempted state jurisdiction, OLA was not able to interview Ms. Austen. However, we obtained documents related to the fraud (including Ms. Austen's plea agreement) and interviewed several officials and employees who worked with Ms. Austen. According to the information we obtained, Ms. Austen established a fictitious vendor in August 2003, and over the course of the next five years, authorized 23 payments to the vendor in amounts ranging from $23,000 to $92,000. She used a process that allowed her to pick up the payments at the Department of Finance and deposit them in her personal bank account. Her scheme was detected when a teller at the bank became suspicious and contacted the state.

Ms. Austen acknowledged her criminal intent in the federal plea agreement. However, OLA's review determined that Ms. Austen was able to perpetrate a fraud over an extended period of time because of internal control weaknesses at the departments of Human Services and Finance (now called Minnesota Management and Budget). Those weaknesses included the following:

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- **Incompatible Access and Duties.** Ms. Austen had incompatible access to the accounting system and had authority to perform incompatible duties. She could:

    - authorize a vendor to be established,
    - authorize payments to the vendor,
    - enter the payments into the accounting system,
    - direct that the payments be held for pick-up, and
    - pick up the payments at the Department of Finance.

  Officials at the Department of Human Services were aware that a significant number of employees, including Ms. Austen, had incompatible access to the accounting system,[1] and at least twice in recent years they took some corrective actions. However, those actions were not sufficient to stop Ms. Austen from improperly obtaining money from the state. In fact, it appears that Ms. Austen used her knowledge of the department's changes to adjust her approach. Starting in October 2007, for example, Ms. Austen reduced the dollar amount of the payments she was obtaining so as not to trigger additional scrutiny that had been established for payments above $25,000. To compensate for the lower amount, Ms. Austen increased the frequency of the fraudulent payments she obtained.

- **Use of General Payment System.** Ms. Austen obtained payments through the state's general payment system, called the Minnesota Accounting and Procurement System (MAPS). It appears she took this approach to avoid controls in the payment system the Department of Human Services normally uses to process vendor Medical Assistance payments, called the Medicaid Management Information System (MMIS). MMIS has controls to verify that payments are being made to legitimate medical providers.

  Officials at the Department of Human Services were aware that some Medical Assistance payments were bypassing MMIS and being made directly through MAPS, but they did not establish controls to mitigate the higher risk of improper payments being made through MAPS. For example, they did not analyze payments or validate them back to information in MMIS. If department officials had routinely reviewed this population of payments, they could have found that the vendor established by Ms. Austen was not a legitimate medical provider and detected the fraud before it reached $1 million.

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[1] For example, OLA's Financial Audit Division issued a report (*Professional/Technical Services Contracts*) in April 2008 that identified several state agencies that had allowed employees to have incompatible access to the state's accounting system without establishing effective controls to monitor transactions processed by those employees. The appendix to the report states that the Department of Human Services had 25 employees with incompatible access to the accounting system.

- **Diversion of Payments from Normal Delivery Process.** One consistent element of this fraud involved Ms. Austen requesting that the Department of Finance hold the payments for her to pick up. While there may be legitimate business reasons for an employee to pick up a payment rather than have it transferred electronically or mailed to the recipient,[2] allowing an employee direct access to a payment creates higher risks that need to be mitigated with additional controls.

  The Department of Finance's form used to request special handling of a state payment requires two signatures and instructs the person making the request to provide a reason why the payment needs to be picked up. In addition, the state's accounting system has a code for payments that are picked up. But there is no evidence that either of these controls ever resulted in anyone at the departments of Human Services or Finance questioning why Ms. Austen was repeatedly picking up payments for the same vendor. Interestingly, the form Ms. Austen used to obtain her final fraudulent payment simply said, "Rush! Kim will pick up."

- **Lack of Follow Up.** In October 2004 and again in October 2005, the fraudulent vendor's tax identification number did not match records at the Internal Revenue Service (IRS). The Department of Finance's efforts to contact the vendor and resolve the discrepancy failed because the vendor did not respond to mailed requests. Although the state did appropriately start to withhold taxes totaling 28 percent from payments to this vendor in April 2005, it did not notify the Department of Human Services that one of its vendors did not have accurate data.

  When the postmaster returned the vendor's 2007 IRS Form 1099[3] to the state because the address was not valid, an official at the Department of Finance contacted the Department of Human Services to obtain a phone number for the vendor. It was provided by Ms. Austen. The Department of Finance official spoke with someone at that number, corrected the address to an address in Florida, and sent out a new IRS Form 1099 for 2007. However, no one at either the Department of Finance or the Department of Human Services followed up to examine the payments made to the vendor or the documentation to support the payments. Whether conducted in 2004 and 2005 when the IRS found the vendor's tax identification number to be inaccurate, or in 2008 when the postmaster returned the vendor's 1099 as undeliverable, such a review would likely have detected the fraud.

[2] A legitimate business need for an employee to pick up a payment might be that the vendor's address has changed or special documents need to accompany the payment.

[3] IRS Form 1099 is used to report payments made to vendors and contractors for tax purposes.

Both the departments of Finance and Human Services have examined the control weaknesses related to Ms. Austen's fraud and indicated that stronger controls are now in place. OLA has not yet audited the changes to determine their effectiveness, but we will as soon as resources and our audit schedule provide us with an opportunity. We will also use what we have learned about the fraud at the Department of Human Services to design future audits we perform at other departments and agencies.

In addition to conducting audits, we will continue to advocate for strong internal controls as we have opportunities to speak with executive officials and staff. We will emphasize management's responsibility to design, implement, and constantly monitor internal controls that protect public money from misuse. While audits are an essential element of accountability and oversight, they are not sufficient to ensure financial integrity in the daily operation of state government. Executive action clearly is necessary. In that regard, we recently developed a "Risk Alert" to help agencies better understand the importance of internal controls and their responsibility to ensure that strong controls are in place. The alert emphasizes the risk of allowing an employee to perform incompatible duties, particularly when the employee has access to payment systems.

OLA's review was conducted by Sonya Johnson, Susan Kachelmeyer, and Melanie Greufe. During our review, we received full cooperation from the departments of Human Services and Finance.

cc: Cal Ludeman, Commissioner, Minnesota Department of Human Services
Tom Hanson, Commissioner, Minnesota Department of Finance

Minnesota Department of **Human Services**

March 19, 2009

James R. Nobles, Legislative Auditor
Office of the Legislative Auditor
Centennial Office Building
658 Cedar Street
St. Paul, MN 55155

Dear Mr. Nobles:

The enclosed material is the Department of Human Services response to the findings and recommendations included in the draft audit report of the financial and compliance audit conducted by your office for the year ended June 30, 2008. It is our understanding that our response will be published in the Office of the Legislative Auditor's final audit report.

The Department of Human Services policy is to follow up on all audit findings to evaluate the progress being made to resolve them. Progress is monitored until full resolution has occurred. If you have any further questions, please contact David Ehrhardt, Internal Audit Director, at (651) 431-3619.

Sincerely,

/s/ Cal R. Ludeman

Cal R. Ludeman
Commissioner

Enclosure

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Department of Human Services
Response to the Legislative Audit Report
For the Year Ended June 30, 2008

Audit Finding #1

The Department of Human Services did not identify, analyze, and document its internal controls related to business operations and the schedules of federal expenditures.

Audit Recommendation #1

The Department of Human Services should continue to review and clearly document its risks, control activities, and internal control monitoring functions for its key business processes.

Department Response #1

The department agrees with the recommendation and will continue to assess, review and document our key business processes.

Person Responsible: Marty Cammack, Financial Operations Director

Estimated Completion Date: September 2009

Audit Finding #2

The Department of Human Services lacked controls over certain financial processes to prevent or detect payments to a fraudulent vendor.

Audit Recommendation #2

The department should strengthen its internal controls over the payment process to ensure:

- adequate separation of incompatible duties, including limitations of system access to employees' specific job responsibilities; and
- valid payments to legitimate vendors

Department Response #2

The department agrees with the recommendation and has revised staff MAPS security parameters within the Central Office Accounts Payable Unit to eliminate all unnecessary and incompatible access. Within State Operated Services, compensating controls are in place to address the remaining situations of MAPS incompatible duties. The department has also taken steps to ensure that payments are both valid and made to actual MMIS vendors.

Person Responsible: Marty Cammack, Financial Operations Director

Estimated Completion Date: Completed

<u>Audit Finding #3</u>

The Department of Human Services did not adequately advise counties about federal compliance and audit requirements.

Recommendation #3-1

The Department of Human Services should properly classify and monitor all of its federal awards to other governmental entities to ensure that subrecipients are aware of program compliance requirements, accurately account for all subgranted federal funds and include those funds in the scope of their annual single audits.

Department Response #3-1

The department agrees with the recommendation. As stated in the audit report, the department has revised the county instruction bulletin for their fiscal year ended December 31, 2008. The counties FY 2008 single audit reports will cover subrecipient federal grant expenditures.

Recommendations #3-2

The Department of Human Services needs to notify the federal Department of Health and Human Services about this significant weakness in its administration of federal funds and determine whether it needs to take additional actions to resolve this issue and if there are any sanctions to the state.

Department Response #3-2

The department agrees with the recommendation. The department has notified the Centers for Medicare and Medicaid Services (CMS) auditors of this weakness. We will work with them to determine the next course of action.

Person Responsible: David Ehrhardt, Internal Audit Director

Estimated Completion Date: September 2009

Auditing Finding #4

The Department of Human Services did not adequately protect not public data on individuals

Audit Recommendation #4

The Department of Human Services should eliminate not public data from the accounting system or work with the Department of Finance to restrict access to the data.

Department Response #4

The Department agrees with the recommendation and is taking steps to ensure that not public data on individuals is protected going forward. The Department will also assist MMB whenever possible in addressing the issue of access to historic data in the IA Warehouse.

Person Responsible: Marty Cammack, Financial Operations Director

Estimated Completion Date: September 2009

Audit Finding #5

Prior Finding Partially Resolved: The Department of Human Services did not validate its federal program payroll costs.

Audit Recommendation #5

The Department of Human Services should continue to review and monitor its federal payroll verification processes to reduce the potential for inaccurate federal payroll certifications and unauthorized activity reports.

Department Response #5

The department agrees with the recommendation and will continue to improve upon its federal payroll verification and activity reporting processes.

Person Responsible: Marty Cammack, Financial Operations Director

Estimated Completion Date: May 1, 2009

Audit Finding #6

Prior Finding Not Resolved: The Department of Human Services submitted reports to the federal government late for three federal programs.

Audit Recommendation #6

The Department of Human Services should improve it reporting process to ensure timely completion of all of its federal reports.

Department Response #6

The department agrees with the recommendation and has made several improvements to its processes in an attempt to improve report submission timing. Unfortunately, given the level of complexity and continuous changes at the federal level, meeting designated timelines will continue to be difficult if not impossible.

Person Responsible: Marty Cammack, Financial Operations Director

Estimated Completion Date: December 2009

Audit Finding #7

The Department of Human Services did not properly record the liability date for nearly $1.3 million of Child Support Enforcement Program's expenditure transactions in the state's accounting system.

Audit Recommendation #7

The Department of Human Services should have a process to record and review the correct liability date in the state's accounting system to ensure accurate financial reporting.

Department Response #7

The department agrees with the recommendation and will ensure that additional training and follow-up are provided to program accountants regarding appropriate procedures for recording the correct liability date during the period of time surrounding end of year and close.

Person Responsible: Marty Cammack, Financial Operations Director

Estimated Completion Date: April 1, 2009

Audit Finding #8

Prior Finding Not Resolved: The Department of Human Services was not in compliance with federal cash management requirements.

Audit Recommendation #8

The Department of Human Services should comply with the federal Cash Management Improvement Act and its Treasury-State Agreement by better monitoring and maintaining minimum program cash balances.

Department Response #8

The department agrees with this recommendation and will monitor the federal program cash balance more closely. The department will perform negative draws when necessary to adjust cash balances, as permitted by the federal letter of credit system. Additional training and follow-up will be provided to program accountants regarding timing of federal draws and submission of payment requests to Accounts Payable staff.

Person Responsible: Marty Cammack, Financial Operations Director

Estimated Completion Date: April 1, 2009

Audit Finding #9

The Department of Human Services did not comply with federal suspension and debarment requirements.

Audit Recommendation #9

The Department of Human Services needs to ensure compliance with federal requirements by verifying suspension and debarment for all federally funded contracts or having vendors certify they are not suspended or debarred.

Department Response #9

The department agrees with the recommendation. We will be adding the suspension and debarment contract language to our FY 2010 annual plan agreements.

Person Responsible: Rae Bly, Appeals and Regulation Director

Estimated Completion Date: June 30, 2009

Audit Finding #10

The Department of Human Services provided federal reimbursements for ineligible adoption assistance services.

Audit Recommendation #10-1

The Department of Human Services needs to review its Adoption Assistance Program's eligibility and payment processes to ensure that it does not make payments for ineligible clients.

Department Response #10-1

The department agrees with the recommendation. The department has reviewed its' process and will develop an extra safeguard within the process. The new process will have two safeguards, a manual look up and a systems data base enhancement.

Person Responsible: Erin Sullivan-Sutton, Child Safety and Permanency Director

Estimated Completion Date: April 15, 2009

Audit Recommendation #10-2

The department needs to recover the questioned costs for the unallowable expenditures.

Department Response #10-2

The expenditures are allowable costs but can not be billed to Title IV-E. Adoption Operation's staff has informed the Financial Operation Division of the children/cases that were not eligible for federal reimbursement. The department will not recover these costs because the private adoption agency is still paid for the services rendered through state not federal funds.

Person Responsible: Erin Sullivan-Sutton, Child Safety and Permanency Director

Estimated Completion Date: March 17, 2009

<u>Audit Recommendation #10-3</u>

The department should review other payments made to this vendor and to other vendors within this program to ensure that it did not incur other unallowable costs.

Department Response #10-3

The department agrees with the recommendation. The department will review contracts with private agencies for 2008 to ensure that similar errors did not occur.

Person Responsible: Erin Sullivan-Sutton, Child Safety and Permanency Director

Estimated Completion Date: April 15, 20009

March 26, 2009

Senator Ann H. Rest, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. Daniel Engstrom, Assistant County Administrator
Hennepin County

We have performed certain audit procedures at Hennepin County as part of our audit of the State of Minnesota's major federal programs for the year ended June 30, 2008. Our work was very limited in scope and was not a comprehensive audit of Hennepin County.

We did this work in conjunction with our audit of the Minnesota Department of Human Services to determine whether the department complied with the federal eligibility requirements applicable to the following federal programs:

- State Children's Health Insurance (CFDA 93.767)
- Medical Assistance (CFDA 93.778)
- Temporary Assistance for Needy Families (CFDA 93.558)

The U.S. Office of Management and Budget's (OMB) *Circular A-133 Compliance Supplement* describes the eligibility requirements for these programs. The compliance supplement requires us to audit recipient eligibility determinations at the county level as part of our audit of the Department of Human Services' benefit payment process. The objectives of our work at Hennepin County were to review internal controls over and compliance with federal eligibility requirements for the redetermination of continued benefits for clients.

As part of our work, we also verified the status of our prior audit findings. Our fiscal year 2007 report (Office of the Legislative Auditor's Financial Audit Division Report 08-12, *Department of Human Services*, issued March 28, 2008) contained two findings addressed to Hennepin County. The county resolved those findings.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in the *Government Auditing Standards*, issued by the Comptroller General of the United States; and the requirements of OMB *Circular A-133 – Audits of States, Local Governments, and Non-Profit Organizations*.

Hennepin County

Hennepin County had the following noncompliance in its fiscal year 2008 eligibility documentation and verification process. We will include these weaknesses in our report to the federal government on compliance with requirements applicable to each State of Minnesota major federal program and internal control over compliance in accordance with OMB *Circular A-133*.

1. Hennepin County did not document the cost effectiveness of other health insurance.

Hennepin County had not determined the cost effectiveness of the other insurance for a Medical Assistance recipient for one of twenty-four cases we tested.[1] Information in the client's file indicated that other insurance was available. Without determining the cost effectiveness of other insurance, neither the state nor the county can ensure that benefits were provided in the most cost effective manner.

As a condition of continued eligibility for the Medical Assistance (CFDA 93.778) benefits, recipients with other health insurance options may be required to enroll or maintain the supplemental insurance if that coverage is deemed to be cost effective. Cost effective coverage is other health care coverage that provides services at a lower premium than the costs the state Department of Human Services would incur if the client was not enrolled in the coverage.[2]

Recommendation

- *Hennepin County should ensure that it determines and documents the cost effectiveness of other health insurance in all cases where the applicant notifies them that other health insurance is available.*

This management letter is intended for the information of the Legislative Audit Commission and the management of Hennepin County. This restriction is not intended to limit the distribution of this report, which was released as a public document on March 26, 2009.

/s/ James R. Nobles

James R. Nobles
Legislative Auditor

/s/ Cecile M. Ferkul

Cecile M. Ferkul, CPA, CISA
Deputy Legislative Auditor

[1] Code of Federal Regulations, 42CFR, Section 433.138-139.
[2] Department of Human Services Health Care Program Manual, Chapter 15.10.05.

Hennepin

Hennepin County Human Services & Public Health Department

Eligibility Support Services
Century Plaza
330 S. 12th Street
Minneapolis, MN 55404

612-348-3540, Phone
612-596-8914, Fax
www.hennepin.us

Mr. James Nobles
Office of the Legislative Auditor
Room 140 Centennial Building
658 Cedar Street
St. Paul, MN 55155-1603

March 18, 2009

Hennepin County has received your letter of March 12, 2009 and has reviewed the finding. The county is in agreement with the finding and accepts the recommendation that Hennepin County should ensure that it determines and documents the cost effectiveness of other health insurance in all cases where the applicant notifies us that other health insurance is available.

As a matter of policy, Hennepin County does in fact determine and document cost effectiveness of other health insurance. This policy was not followed in the case cited by the auditor as a result of an oversight by a county worker. This finding will be shared with managers and supervisors and this policy will be reviewed at staff meetings within the next month. The person responsible for implementation of this corrective action plan is Tom Pingatore.

Sincerely,

Tom Pingatore

Tom Pingatore, 612-348-3540
Human Services Program Manager

OLA
OFFICE OF THE LEGISLATIVE AUDITOR
State of Minnesota • James Nobles, Legislative Auditor

March 26, 2009

Senator Ann H. Rest, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. Monty Martin, Director of Human Services
Ramsey County

We have performed certain audit procedures at Ramsey County as part of our audit of the State of Minnesota's major federal programs for the year ended June 30, 2008. Our work was very limited in scope and was not a comprehensive audit of Ramsey County.

We did this work in conjunction with our audit of the Minnesota Department of Human Services to determine whether the department complied with the federal eligibility requirements applicable to the following federal programs:

- State Children's Health Insurance (CFDA 93.767)
- Medical Assistance (CFDA 93.778)
- Temporary Assistance for Needy Families (CFDA 93.558)

The U.S. Office of Management and Budget's (OMB) *Circular A-133 Compliance Supplement* describes the eligibility requirements for these programs. The compliance supplement requires us to audit recipient eligibility determinations at the county level as part of our audit of the Department of Human Services' benefit payment process. The objectives of our work at Ramsey County were to review internal controls over and compliance with federal eligibility requirements for the redetermination of continued benefits for clients.

As part of our work, we also verified the status of our prior audit findings. Our fiscal year 2007 report (Office of the Legislative Auditor's Financial Audit Division Report 08-12, *Department of Human Services*, issued March 28, 2008) contained two findings addressed to Ramsey County. The county did not resolve those finding, and they are repeated in this management letter as Findings 1 and 2.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in the *Government Auditing Standards*, issued by the Comptroller General of the United States; and the requirements of OMB *Circular A-133 – Audits of States, Local Governments, and Non-Profit Organizations*.

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Ramsey County

Ramsey County had the following noncompliance in its fiscal year 2008 eligibility documentation and verification process. We will include these weaknesses in our report to the federal government on compliance with requirements applicable to each State of Minnesota major federal program and internal control over compliance in accordance with OMB *Circular A-133*.

1. Prior Finding Not Resolved: Ramsey County did not resolve income discrepancies identified as part of the benefit eligibility process in the timeframes required by federal regulations.

Ramsey County has not attained the rate of income discrepancy resolution required by federal regulations. For the period July 1, 2007, through June 30, 2008, Ramsey County's overall resolution rate was 68.5 percent. The county's resolution rates in fiscal years 2007 and 2006 were 67.8 percent and 71.6 percent, respectively. Federal law requires the state to resolve at least 80 percent of the case discrepancies within 45 days. To achieve the state's compliance, the Department of Human Services relies on county human services offices to review and resolve these discrepancies.

The Department of Human Services identifies income discrepancies through the Income Eligibility and Verification System (IEVS). This system coordinates data exchanges with other sources for the Temporary Assistance for Needy Families (CFDA 93.558) and the Medical Assistance (CFDA 93.778) programs. The IEVS system compares income information submitted by applicants with income and tax information obtained from other state and federal sources, such as the Minnesota Department of Employment and Economic Development, the Social Security Administration, and the Internal Revenue Service. Discrepancies occur when the income amounts recorded in the state's eligibility determination system differ by more than a pre-established target amount. The Department of Human Services provides these income discrepancies to the counties for investigation and resolution.

Recommendation

- *Ramsey County should continue to work with the Department of Human Services to resolve Income Eligibility Verification System discrepancies in a timely manner.*

2. Prior Finding Not Resolved: Ramsey County did not comply with citizenship verification requirements.

Ramsey County did not comply with federal regulations that require, as a condition of eligibility, all applicants to furnish citizenship documentation when applying for Medical Assistance (CFDA 93.778) and other health care programs. Ramsey County did not have evidence of citizenship documentation in the file for five out of twenty-one applicants that we tested.

According to regulations provided by the Center for Medicare and Medicaid Services, as of July 1, 2006, applicants must provide U.S. citizenship and identity documentation as a condition of original and continued eligibility for federal medical assistance benefits, which also impacts eligibility for the state's MinnesotaCare program for families with children, and the Minnesota Family Planning Program. Not having citizenship documentation, as required by federal regulations, could make applicants ineligible for program benefits.

Recommendation

- *Ramsey County should ensure that proper citizenship documentation is obtained for all health care program applicants.*

This management letter is intended for the information of the Legislative Audit Commission and the management of Ramsey County. This restriction is not intended to limit the distribution of this report, which was released as a public document on March 26, 2009.

/s/ James R. Nobles	*/s/ Cecile M. Ferkul*
James R. Nobles Legislative Auditor	Cecile M. Ferkul, CPA, CISA Deputy Legislative Auditor

Ramsey County

Community Human Services Department

160 Kellogg Blvd. E.
St. Paul, MN 55101-1494

Financial TDD: 651-266-3750
Services TDD: 651-266-4002
General Info: 651-266-4444

James R. Nobles
Legislative Auditor
Office of The Legislative Auditor
Room 140 Centennial Building
658 Cedar Street
St Paul, MN 55155-1603

March 19, 2009

Dear Mr. Nobles:

We have received the draft management letter summarizing the results of our audit for the year ended June 30, 2008. The following issues have been identified as needing resolution.

1. PRIOR FINDING NOT RESOLVED: Ramsey County did not resolve income discrepancies identified as part of the benefit eligibility process in the time frames required by federal regulations.

Ramsey County acknowledges that we have not met the standard for IEVS processing and that our performance has not improved in this aspect. Our goal is to be in compliance and to that end we continue to look at how we can achieve that goal. Some of the steps we have taken are as follows.

1. In Family Case Management one supervisor and some of her staff are focusing on IEVS for the entire section. They work off a report that we are able to produce internally and format in a way we find useful. For example it identifies the oldest matches first.
2. This same report is also split by unit and each unit supervisor in Family Case Management receives a copy and follows up as needed. By being able to clearly see each unit's activity level the manager and the supervisor are able to identify problem areas and work on improving compliance in that unit and/or with specific workers.
3. We have a new training unit and they have revised the IEVS training packet and will provide the training for new workers and refresher training for other staff.
4. We are working with staff in our records department to ensure that closed cases are reviewed for outstanding IEVS matches and are rejected back to the worker rather than filed in closed records. Staff does have a check off sheet that includes reviewing for unresolved IEVS matches. However as some matches seem to appear after the case is in closed files we are listing them on our internal report for review and resolution.

2. PRIOR FINDING NOT RESOLVED: Ramsey County did not comply with citizenship verification requirements.

We recognize that as part of processing all federal Medical Assistance applications we are required to obtain citizenship documentation, and without such documentation we have not proven eligibility. We have provided clear expectations to staff in regards to obtaining the proper documentation at intake and at other appropriate times. We implemented a number of steps (as outlined in our 2008 response) that we think have been effective but as a number of the cases that were reviewed actually closed in 2007 or early 2008 this audit may not reflect those efforts. As part of our continuing efforts we are also taking the following steps.

1. We will continue to do targeted case reviews for citizenship/identity. We have an on-line case review data base system specifically designed for doing this.
2. We will use the information from the reviews to deal with specific situations and to help us develop cheat sheets and training. For example, we have identified adding newborns as one area needing more emphasis.
3. We are reissuing our Policy and Procedure memo with updated clarifications.

Cristy Hong and Nancy Cincotta are the managers who are responsible for overseeing on-going compliance with these plans.

Sincerely,

/s/ Mary Nelson

Mary Nelson

Division Director