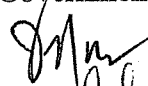
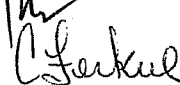


OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA • James Nobles, Legislative Auditor

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:

- **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.

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 1099³ 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.

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

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.

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