



OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

Financial-Related Audit

Department of Human Services
Fiscal Year Ended June 30, 2001



Financial Audit Division

The Office of the Legislative Auditor (OLA) is a professional, nonpartisan office in the legislative branch of Minnesota State government. Its principal responsibility is to audit and evaluate the agencies and programs of state government (the State Auditor audits local governments).

OLA's Financial Audit Division annually audits the state's financial statements and, on a rotating schedule, audits agencies in the executive and judicial branches of state government, three metropolitan agencies, and several "semi-state" organizations. The division also investigates allegations that state resources have been used inappropriately.

The division has a staff of approximately fifty auditors, most of whom are CPAs. The division conducts audits in accordance with standards established by the American Institute of Certified Public Accountants and the Comptroller General of the United States.

Consistent with OLA's mission, the Financial Audit Division works to:

- Promote Accountability,
- Strengthen Legislative Oversight, and
- Support Good Financial Management.

Through its Program Evaluation Division, OLA conducts several evaluations each year and one best practices review.

OLA is under the direction of the Legislative Auditor, who is appointed for a six-year term by the Legislative Audit Commission (LAC). The LAC is a bipartisan commission of Representatives and Senators. It annually selects topics for the Program Evaluation Division, but is generally not involved in scheduling financial audits.

All findings, conclusions, and recommendations in reports issued by the Office of the Legislative Auditor are solely the responsibility of the office and may not reflect the views of the LAC, its individual members, or other members of the Minnesota Legislature.

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If you have comments about our work, or you want to suggest an audit, investigation, evaluation, or best practices review, please contact us at 651-296-4708 or by e-mail at auditor@state.mn.us



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

Senator Ann H. Rest, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. Michael O'Keefe, Commissioner
Department of Human Services

We have audited selected areas of the Department of Human Services for the period July 1, 2000, through June 30, 2001, as further explained in Chapter 1. Our audit scope included the department's expenditures for payroll, professional service contracts, rent, employee travel expense reimbursements, and licensing revenue. The audit objectives and conclusions are highlighted in the individual chapters of this report. We emphasize that this has not been a comprehensive audit of all of the Department of Human Service's financial activities.

We conducted our audit in accordance with *Government Auditing Standards*, as issued by the Comptroller General of the United States. Those standards require that we obtain an understanding of management controls relevant to the audit. The standards require that we design the audit to provide reasonable assurance that the Department of Human Services complied with provisions of laws, regulations, contracts, and grants that are significant to the audit. Management of the Department of Human Services is responsible for establishing and maintaining the internal control structure and complying with applicable laws, regulations, contracts, and grants.

This report is intended for the information 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 21, 2002.

/s/ James R. Nobles

James R. Nobles
Legislative Auditor

/s/ Claudia J. Gudvangen

Claudia J. Gudvangen, CPA
Deputy Legislative Auditor

End of Fieldwork: February 8, 2002

Report Signed On: March 15, 2002

Department of Human Services

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Audit Participation

The following members of the Office of the Legislative Auditor prepared this report:

Claudia Gudvangen, CPA	Deputy Legislative Auditor
Jeanine Leifeld, CPA, CISA	Audit Manager
Michael Hassing, CPA	Audit Director
Carl Otto, CPA	Team Leader
Kathy Fisher	Auditor
Gena Hoffman	Auditor
Alan Sasse	Auditor
Richard Stroncek	Auditor
Rob Litchke	Intern

Exit Conference

We discussed the findings and recommendations with the following representatives of the Department of Human Services at the exit conference held on February 28, 2002:

Dennis Erickson	Assistant Commissioner
Jon Darling	Director of Financial Management
David Ehrhardt	Internal Audit Director

Report Summary

The Department of Human Service's internal controls provided reasonable assurance that it accurately recorded financial activity for the department's payroll, rent, professional services contracts, employee travel expense reimbursements, and licensing revenue in the state's accounting and payroll systems. For the items tested, except for the site visits discussed below, the department complied with applicable legal provisions.

Key Findings and Recommendations

- The department did not independently verify payroll transactions entered into the payroll system. We recommended that the department develop procedures to independently verify payroll transactions processed in the state's payroll system. (Finding 1, page 5)
- The department did not conduct site visits to licensees on a timely basis, as required by state statutes. We recommended that the department's licensing division should perform monitoring in accordance with established guidelines and legal requirements. (Finding 2, page 10)

Agency Background

The Department of Human Services (DHS) helps people, including families, children, and senior citizens, meet their basic needs. The department works in conjunction with employees from Minnesota's 87 counties who provide most of the direct services to the state's needy citizens. The department has an annual budget of approximately \$6.5 billion. Michael O'Keefe is the current commissioner of the department, which has approximately 6,700 employees.

Financial-Related Audit Reports address internal control weaknesses and noncompliance issues found during our audits of state departments and agencies. The scope of our audit of selected department activities in this report was supplemental to the audit work performed as part of the annual statewide audit, the purpose of which is to render an opinion on the State of Minnesota's financial statements for fiscal year 2001. In a separately issued management letter to the Department of Human Services, we identified two issues related to eligibility verification and monitoring that we reported as the result of our statewide audit work.

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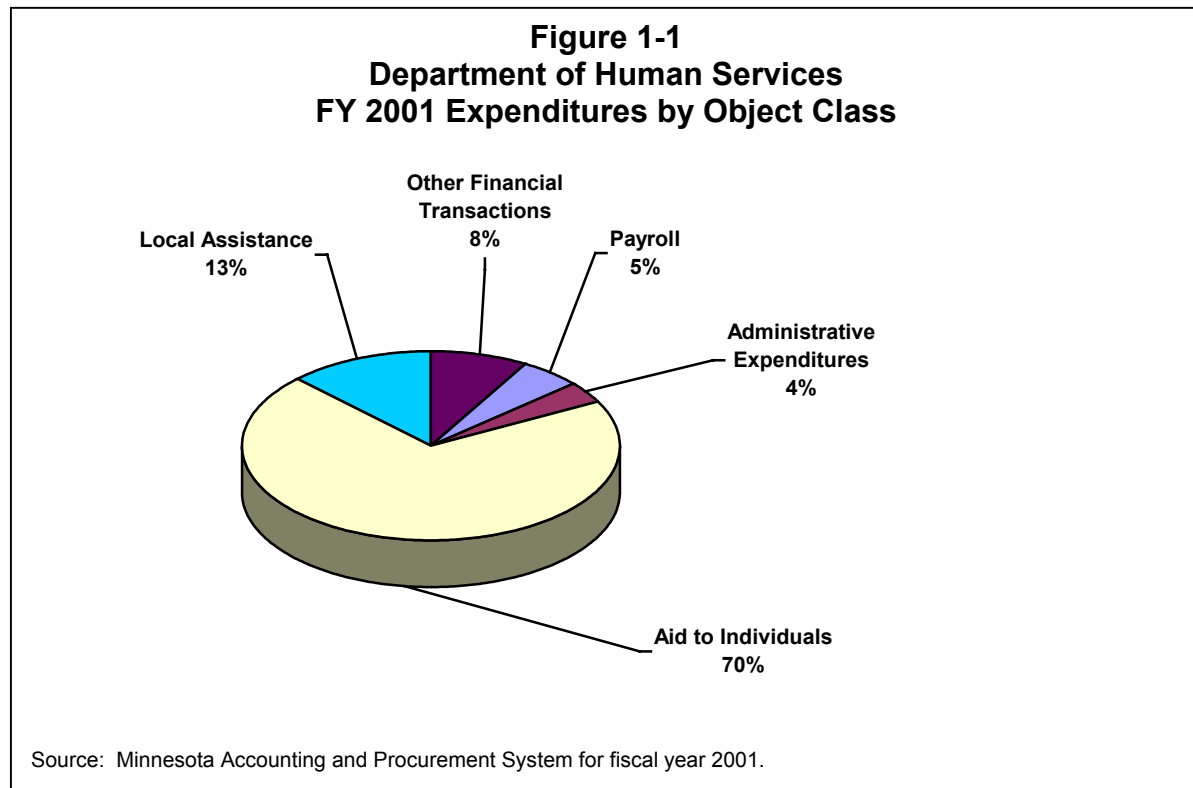
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Chapter 1. Introduction

The Department of Human Services (DHS) helps people, including families, children, and senior citizens, meet their basic needs. The department works in conjunction with employees from Minnesota's 87 counties who provide most of the direct services to the state's needy citizens.

The department is organized around four main business functions: Economic and Community Support Strategies, Health Care, State Operated Services, and Continuing Care. The department also manages the Aging Initiative, Children's Services, Finance and Management Operations, and other agency-wide functions. The current commissioner of the agency is Michael O'Keefe.

The department spent over \$6.5 billion in fiscal year 2001. As shown in Figure 1-1, the majority of the expenditures were for aid to individuals and local governmental units. The department's main funding sources consist of General Fund appropriations and federal grants, supplemented by third-party fees for services, insurance payments, child support payments, and other reimbursements.



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The current audit was supplemental to the work we performed during our annual Statewide Audit of the state's financial statements and material federal programs. We focused our statewide audit work at the Department of Human Services on the material grant and assistance programs, such as Medical Assistance, Temporary Assistance for Needy Families (TANF), Child Support, and social service aids paid to local governments. We reported the results of our work on these programs in a separately issued management letter to the department.

We focused the current audit on selected departmental activities including payroll, rent, professional and technical service contracts, employee travel expenses, and licensing. Table 1-1 shows the financial activity the department recorded for these areas during fiscal year 2001.

Table 1-1
Department of Human Services
Selected Scope Audit Areas
FY 2001

Administrative Expenditures:	
Payroll	\$335,271,114
Professional Technical Contracts (Non-state Vendors)	30,997,798
Rent	12,016,445
Employee Travel Expenses and Motor Pool	3,726,947
Licensing Revenue	1,801,106

Source: Minnesota Accounting and Procurement System for fiscal year 2001.

Chapter 2. Payroll

Chapter Conclusions

For the items tested, the Department of Human Services complied with applicable finance-related legal requirements and provisions of compensation plans and bargaining unit agreements. The internal controls at the central office provided reasonable assurance that payroll expenditures were accurately recorded in the accounting and payroll systems, and that employees were compensated in compliance with legal provisions and management's authorization. However, we noted that the department did not verify the accuracy of the biweekly payroll register report.

Payroll is the Department of Human Services' largest administrative expenditure, totaling approximately \$335 million in fiscal year 2001. This represents about five percent of the department's annual budget. The department is the largest agency in the state and employed approximately 6,700 individuals statewide during our audit period. Due to the number of employees and the diverse nature of the department's operations, the department has many staff involved in the payroll process. The agency's financial management division is responsible for processing the biweekly payroll for the central office employees. However, the regional treatment centers, state nursing home, and state operated services are responsible for processing their own payroll transactions. The department compensates employees according to the provisions of a wide variety of bargaining unit agreements and compensation plans.

Audit Objectives and Methodology

Our audit of payroll expenditures focused on the following objectives:

- Did the department comply with significant finance-related legal requirements, compensation plans, and bargaining unit agreements?
- Did the internal controls at the central office provide reasonable assurance that payroll expenditures were accurately recorded in the accounting and payroll systems, and that employees were paid in compliance with legal provisions and management's authorization?

To address these objectives, we tested a sample of agency-wide employee payroll transactions for proper documentation and authorization for hours worked and leave taken. We analyzed the payroll population for reasonableness of employee salaries, significant pay rate changes, and special types of payroll transactions. We also verified that the department ensured that staff had the appropriate system security clearances related to current payroll responsibilities. Finally, we

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obtained an understanding of the internal control structure in place over the processing of payroll expenditures at the central office.

Conclusions

For the items tested, the Department of Human Services complied with applicable finance-related legal requirements and provisions of compensation plans and bargaining unit agreements. The internal controls at the central office provided reasonable assurance that payroll expenditures were accurately recorded in the accounting and payroll systems, and that employees were compensated in compliance with legal provisions and management's authorization. However, as discussed in Finding 1, we found that the department did not perform an independent verification of transactions entered into the payroll system.

1. The central office did not independently verify payroll transactions entered into the payroll system.

The central office did not perform an independent verification of transactions entered into the state's payroll system (SEMA4). Many staff persons enter hours worked and leaves taken from employee timesheets. They also enter special lump sum or retroactive payroll adjustment transactions. However, no one independent of the payroll process reviews the output reports for errors.

Department staff can use the payroll register report to verify the accuracy of the input of employee timesheet hours, pay rates, and special transactions into SEMA4. SEMA4 Operating Policy and Procedure PAY0028 requires agencies to perform an independent review of the payroll register. This review is intended to ensure that payroll entry errors and labor distribution errors do not occur, or are detected and corrected in a timely manner.

Recommendation

- *The central office should develop procedures to provide for an independent verification of payroll transactions processed in SEMA4.*

Chapter 3. Selected Administrative Expenditures

Chapter Conclusions

The Department of Human Services internal controls provided reasonable assurance that administrative expenditures for professional and technical contracts, rent, and employee travel expenses were accurately recorded in the accounting systems, and that contractors and employees were compensated in compliance with legal provisions and management's authorization. For the items tested, the department complied with applicable finance-related legal requirements, statewide policies, and the compensation plan provisions covering administrative expenditures.

In addition to payroll, the department incurred significant administrative costs related to professional and technical service contracts, rent, and travel. Expenditures for these areas totaled approximately \$47 million in fiscal year 2001. Table 3-1 shows the selected administrative expenditure categories included in our audit scope.

Table 3-1
Department of Human Services
Selected Administrative Costs
Fiscal Year 2001

	<u>2001</u>
Professional and Technical Contracts: ⁽¹⁾	
Special Revenue Fund	\$16,059,431
General Fund	9,329,471
Federal Fund	3,586,507
Other Funds	<u>2,022,391</u>
Total	\$30,997,800
Rent	12,016,445
Travel	<u>3,726,947</u>
Total Selected Administrative Costs	<u>\$46,741,192</u>

Note (1) Includes contracts to non-state vendors only.

Source: Minnesota Accounting and Procurement System for fiscal year 2001.

Professional and Technical Contractual Services

The department spent approximately \$31 million on professional and technical contracts to non-state vendors during fiscal year 2001. The department obtains a wide range of services through the contract process, such as analysis of financial systems, program consulting services, and specialized medical reviews and certifications.

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The Contracts Section of the Appeals and Regulations Division coordinates and reviews contracts for the department. The department has developed a contract manual that outlines the department's contracting policies and procedures. The financial management staff monitors grant awards, draws federal cash as needed to pay claims, verifies invoice authorizations, and processes payments for professional services contracts.

Rent

The department incurred approximately \$12 million in rental costs for non-state owned facilities during fiscal year 2001. The department leases the majority of its office space in the metropolitan area. The department also operates regional treatment centers, a state nursing home, and numerous homes that serve as permanent and transitional housing for various clients with disabilities. The management services division monitors and manages the leases and approves lease payments for the central office and metro area facilities.

The central office, located at 444 Lafayette Road in Saint Paul, houses the majority of the department's employees. The department rents additional office space for six divisions of the department at the following locations in the metro area:

- | | |
|-----------------------------------|--|
| • Child Support Enforcement | Metro Square, 121 E. Seventh Place, St. Paul |
| • Continuing Care Division | 2284 Highcrest Road, Roseville |
| • Deaf & Hard of Hearing Services | Metro Annex, 130 E. Seventh Street, St. Paul |
| • Licensing | 444 Pine Street, St. Paul |
| • Minnesota Care | Commerce Building, 8 East 4 th Street, St. Paul |
| • Health Care Strategies | 800 Minnehaha Avenue, St. Paul |

Travel Expenditures

The department spent approximately \$3 million on travel activities during fiscal year 2001. Of that amount, the department incurred motor pool charges of approximately \$1.5 million and employee travel reimbursements for lodging, meals, and mileage of approximately \$1.4 million. The remaining travel costs were for direct charges for airline tickets, hotel costs, and board member travel reimbursements.

The accounts payable unit of the Financial Management Division processes payments into the accounting system (MAPS) for motor pool charges and non-employee travel costs, and into the payroll system (SEMA4) for employee travel reimbursements. The department follows the Department of Administration's travel guidelines and reimburses employees according to the reimbursement rates established in the various bargaining unit agreements.

Audit Objectives and Methodology

Our audit of selected non-payroll administrative expenditures focused on the following objectives:

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- Did the department's internal controls provide reasonable assurance that payments for professional and technical contracts, rent, and travel expenditures were accurately recorded in the accounting system, and that contractors and employees were paid in compliance with legal provisions and management's authorization?
- Did the department comply, in all material respects, with significant finance-related legal requirements, statewide policies, and compensation plan provisions covering administrative expenditures?

To meet these objectives, we obtained an understanding of the internal control structure in place over the processing of the department's professional and technical contracts, rent, and employee travel expenditures. We reviewed a sample of expenditure transactions in each area to determine if they were properly authorized, processed, and recorded. We also reviewed expenditures to determine if the department complied with applicable finance-related legal provisions.

Conclusions

The Department of Human Services' internal controls provided reasonable assurance that administrative expenditures for professional and technical contracts, rent, and employee travel expenditures were accurately reported in the accounting records and in compliance with applicable legal provisions and management's authorization. For the items tested, the department complied with the applicable finance-related legal requirements, compensation plan provisions covering statewide policies, and administrative expenditures.

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Chapter 4. Licensing Receipts

Chapter Conclusions

The Licensing Division's internal controls provided reasonable assurance that it properly recorded its financial activity and adequately safeguarded its assets. However, we found that the division did not make the required site visits to licensees on a timely basis. For the items tested, the division complied with other material finance-related legal and policy provisions.

The department's licensing division issues licenses to approximately 3,800 direct monitored programs, such as chemical dependency programs, child care centers, and rehabilitation programs for persons with disabilities. Minnesota counties also monitor certain types of licensees, but the department is not responsible for licensing the county monitored programs. In addition, the division performs over 170,000 background studies a year on individuals providing direct contact services in facilities licensed by the Departments of Human Services and Health.

The department received approximately \$1.8 million during fiscal year 2001 from licensing, fines, and interagency payments for the background studies. The department's fee structure is established in state statute and rules. The department deposits revenue from licenses and fines to the general fund as non-dedicated receipts. The department uses funds from interagency agreements for operations.

The licensing division uses the License Information System to track licenses issued, amounts billed and received, and licensee history. The licensing system interfaces with the accounts receivable system in the state's accounting system (MAPS). The department issues licenses annually on a calendar year basis.

Audit Objectives and Methodology

We focused our review of license receipts on the following objectives:

- Did the department's internal controls provide reasonable assurance that the appropriate amount of license revenue was collected, adequately safeguarded, and properly reported in the accounting records?
- Did the department comply with applicable legal and policy provisions related to licensure?

To address these objectives, we interviewed license division staff to gain an understanding of the licensing process, including invoicing, collecting and depositing receipts, issuing licenses, and

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monitoring outstanding accounts. In addition, we selected a sample of receipt transactions and verified whether staff properly collected, adequately safeguarded, and properly reported the appropriate license fee. We also verified compliance with site visit monitoring requirements and other applicable legal provisions.

Conclusions

We found that the department's internal controls provided reasonable assurance that it accurately reported its licensing receipts in the accounting records. As discussed in Finding 2, we found that the department did not perform site visits of licensees on a timely basis, as required by state law. For the items tested, the department complied with other applicable finance-related legal provisions.

2. The department did not conduct site visits to licensees on a timely basis, as required by state statutes.

The department did not conduct routine site visits of licensed programs every two years as required by Minn. Stat. Section 245A.04, Subd. 7. In addition, the department did not visit all newly licensed programs within one year of the initial license, as required by Minn. Stat. Section 245A.04, Subd. 4. Site visits help ensure that programs and facilities are in compliance with applicable laws and regulations.

The department is responsible for licensing approximately 3,800 direct monitored programs, such as child care centers, chemical dependency programs, and residential programs for persons with disabilities. According to the department, one-third of the department's monitored programs have not received a routine licensing visit within the past 24 months.

Recommendation

- *The department's Licensing Division should monitor programs in accordance with established guidelines and legal requirements.*

**Status of Prior Audit Issues
As of February 8, 2002**

March 14, 2002, Legislative Audit Report 02-15 examined the Department of Human Services activities and programs material to the State of Minnesota's general purpose financial statements for the fiscal year ended June 30, 2001. The report contained two issues related to weaknesses in internal control or noncompliance with federal requirements related to eligibility verification and monitoring.

March 8, 2001, Legislative Audit Report 01-10 examined the Department of Human Services activities and programs material to the State of Minnesota's general purpose financial statements for the fiscal year ended June 30, 2000. The report contained two findings concerning weaknesses in internal control. The department has resolved both of the issues.

March 1, 2001 Legislative Audit Special Review: State Paid Per Diems Report 01-05 identified one member of the department's Board on Aging who had inappropriately received per diem payments. The department has resolved this issue.

State of Minnesota Audit Follow-Up Process

The Department of Finance, on behalf of the Governor, maintains a quarterly process for following up on issues cited in financial audit reports issued by the Legislative Auditor. The process consists of an exchange of written correspondence that documents the status of audit findings. The follow-up process continues until Finance is satisfied that the issues have been resolved. It covers entities headed by gubernatorial appointees, including most state agencies, boards, commissions, and Minnesota state colleges and universities. It is not applied to audits of the University of Minnesota, any quasi-state organizations, such as the metropolitan agencies, or the State Agricultural Society, the state constitutional officers, or the judicial branch.

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March 13, 2002

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 audit of selected programs of the Department of Human Services conducted by your office for the year ended June 30, 2001. 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) 282-9996.

Sincerely,

/s/ Michael O'Keefe

Michael O'Keefe
Commissioner

Enclosure

cc: Jeanine Leifeld
Michael Hassing

**Department of Human Services
Response to the Legislative Audit Report on
Selected Programs For the Year Ended June 30, 2001**

Audit Finding #1

The central office did not independently verify payroll transactions entered into the payroll system.

Audit Recommendation #1

The central office should develop procedures to provide for an independent verification of payroll transactions processed in SEMA4.

Department Response #1

We agree with the recommendation. When SEMA4 was implemented Financial Management decentralized payroll input. Initially Financial Management did a "sample" audit (at least one Division) of payroll each pay-period. Financial Management has immediately restored auditing one or more Division's payroll each pay-period. The sample audit encompasses comparing the payroll register report to timesheets to assure accurate input and a review to ensure that payroll policy is consistently adhered to across central office.

Person Responsible: Jon Darling, Director, Financial Management Division

Estimated Completion Date: Implemented 3/1/2002

Audit Finding #2

The department did not conduct site visits to licensees on a timely basis, as required by state statutes.

Audit Recommendation #2

The department's Licensing Division should monitor programs in accordance with established guidelines and legal requirements

Department Response #2

The department agrees with the recommendation. During the last budget session, the department requested and received additional funding to increase the division's staff to address the need for more timely completion of licensing reviews. We were in the process of hiring additional staff when H.F. 351 was enacted. Until the hiring freeze is lifted the department will not be able to hire licensing staff.

Person Responsible: Jerry Kerber, Director, Licensing Division

Estimated Completion Date: Unknown due to the hiring freeze.