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STATE OF MINNESOTA

FINANCIAL AUDIT DIVISION REPORT

Department of Health
Federal Compliance Audit
Year Ended June 30, 2008

March 26, 2009

Report 09-06

FINANCIAL AUDIT DIVISION

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OFFICE OF THE LEGISLATIVE AUDITOR

State of Minnesota • James Nobles, Legislative Auditor

March 26, 2009

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Legislative Audit Commission

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Dr. Sanne Magnan, Commissioner
Minnesota Department of Health

This report presents the results of our audit of certain federal financial assistance programs administered by the Department of Health 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 Health.

We discussed the results of the audit with department staff at an exit conference on March 11, 2009. The audit was conducted by Amy Jorgenson, CPA, (Audit Manager) and Tracy Gebhard, CPA, (Auditor-in-Charge), assisted by auditors Lat Anantaphong, Bridgette Leonard, and Lindsay Tietze.

This report is intended for the information and use of the Legislative Audit Commission and the management of the Department of Health. 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

James R. Nobles
Legislative Auditor

/s/ Cecile M. Ferkul

Cecile M. Ferkul, CPA, CISA
Deputy Legislative Auditor

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Report Summary

Conclusion

The Department of Health generally complied with and had controls to ensure compliance with certain provisions of laws, regulations, contracts, and grants applicable to the major federal programs we audited for fiscal year 2008. However, the department had several internal control weaknesses as noted in the six findings presented in this report.

Findings

- The department did not identify, analyze, and document their internal controls related to business operations and schedule of federal expenditures. ([Finding 1, page 5](#))
- Prior Finding Partially Resolved: The department did not comply with federal requirements for documenting time charged to federal programs. ([Finding 2, page 6](#))
- Prior Finding Partially Resolved: The department did not accurately report financial activity on the Schedule of Expenditures of Federal Awards. ([Finding 3, page 7](#))
- The department allowed employees to have incompatible access to the state's accounting system without establishing mitigating controls. ([Finding 4, page 8](#))
- Prior Finding Partially Resolved: The department did not monitor subrecipient activity, as required by federal regulations. ([Finding 5, page 9](#))
- The department did not comply with federal suspension and debarment requirements. ([Finding 6, page 10](#))

Audit Scope

We audited these programs which were material to the State of Minnesota's federal program compliance for fiscal year 2008:

- Special Nutrition Program: Women, Infants and Children (CFDA 10.557)
 - Centers for Disease Control and Prevention – Investigations and Technical Assistance (CFDA 93.283)
 - Childhood Immunization Grants (CFDA 93.268)
-

Department of Health

Federal Program Overview

The Department of Health 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 federal programs.

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

<u>CFDA¹</u>	<u>Program Name</u>	<u>Expenditures</u>
10.557	Special Nutrition Program for Women, Infants and Children	\$93,925,312
93.283	Centers for Disease Control and Prevention - Investigations and Technical Assistance ²	\$28,161,548
93.268	Childhood Immunization Grants ³	\$31,789,701

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

²Includes the Public Health Preparedness and Response to Bioterrorism Program.

³Childhood Immunization federal expenditures include \$27.4 million of vaccinations and \$4.5 million of financial assistance.

Source: Selected accounting transactions within the Minnesota Accounting and Procurement System for fiscal year 2008 and Minnesota Department of Health summary of vaccinations received from the Centers for Disease Control.

Objectives, Scope, and Methodology

The objective of our audit was to determine whether the Department of Health 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

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.

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, the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and with the U.S. Office of Management and Budget's *Circular A-133* for audits of federal programs.

Conclusion

The Department of Health generally complied with and had controls to ensure compliance with certain provisions of laws, regulations, contracts, and grants applicable to the major federal programs we audited for fiscal year 2008. However, the department had some weaknesses, as noted in the following *Findings and Recommendations* section.

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.

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.)

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

The Minnesota Department of Health did not identify, analyze, and document their internal controls related to business operations and schedule of federal expenditures.

Finding 1

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

State policy states that each agency head has the responsibility to identify, analyze, and manage business risks that impact an entity's ability to maintain its financial strength and the overall quality of its products and government services.⁴ This policy also requires communication of the internal control policies and procedures to all staff so they understand what is expected of them 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 executive management and those individuals in a position to take corrective action. A new audit standard⁵ 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 Minnesota Department of Health is aware of certain risks, has many control activities in place, and performs selected internal control monitoring functions. However, the department has not comprehensively identified and analyzed the risks, designed its controls to address significant risks, or developed monitoring procedures to ensure the controls are in place and are effective to reduce the significant risks identified.

Findings 2 through 6 identify deficiencies in the department's internal control procedures and specific noncompliance with federal requirements which were not prevented or detected by the department's internal control structure. If the department had a comprehensive internal control structure, it should have identified these deficiencies, assessed the degree of risk of these deficiencies, designed control procedures to address significant risks, and monitored whether controls were working as designed and effective in reducing the risks to an

⁴ Minnesota Department of Finance Policy Number 0102-01.

⁵ Statement on Auditing Standards #109.

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 should regularly review and clearly document its risks, control activities, and internal control monitoring functions for its key business processes.*

Finding 2

Prior Finding Partially Resolved:⁶ The Department of Health did not comply with federal requirements for documenting time charged to federal programs.

The department did not provide sufficient oversight or adequately document the basis for payroll costs charged to the Childhood Immunization (CFDA 93.268) and Centers for Disease Control Technical Assistance (CFDA 93.283) programs. The department created new policies and procedures for documenting time charged to federal programs but did not put them into effect until the beginning of state fiscal year 2009.

First, the department continued to have problems supporting its payroll charges to specific federal programs. Federal regulations require employees who work on multiple programs to support the allocation of their salaries among funding sources with personnel activity reports or equivalent documentation.⁷ This documentation must reflect the actual activity of each employee and account for the total activity for which each employee is compensated. Additionally, when employees are assigned to work on only one federal program, charges for their salaries must be supported by periodic certifications that the employee worked solely on that program. Our testing of the department's documentation to support time charged by 20 employees to the three major federal programs in our audit scope identified the following problems:

- Three employees did not complete any time studies or certifications during fiscal year 2008.
- Two other employees did not have the required number of time studies or certifications on file.

⁶ Unless otherwise noted, all prior audit findings mentioned in this report are from the Office of the Legislative Auditor's Financial Audit Division Report 08-10, *Department of Health Federal Program Compliance*, issued March 20, 2008.

⁷ U.S. Office of Management and Budget Circular A-87, *Cost Principles for State, Local, and Indian Tribal Governments*.

- Eight employees had time studies that did not match the actual time charged to each federal funding source.
- Three employees lacked sufficient documentation to support the time charged.

Second, the department continued to make significant manual adjustments to its payroll transactions. State policy⁸ states that mass expense transfers are not intended as a means to correct a recurring problem. When employees submit time studies, the department adjusts the default funding allocations to more accurately account for time charged to federal programs. Manual adjustments create additional workload for the department and increase the risk of error. The department implemented a new policy effective July 1, 2008, to charge time to federal programs based on actual hours worked by employees rather than relying on default allocations.

Recommendation

- *The department should provide oversight of its payroll process to ensure compliance with federal and state requirements for documenting time charged to specific programs by:*
 - *Educating all supervisors, federal grant program managers, and employees about the requirements for documenting time charged to federal programs.*
 - *Monitoring that all employees, as required, complete time studies and certifications timely and provide sufficient federal payroll documentation to the central accounting unit.*
 - *Determining whether its new policy has reduced the need for manual adjustments to payroll charged to its federal programs.*

Prior Finding Partially Resolved:⁹ The Department of Health did not accurately report financial activity on the Schedule of Expenditures of Federal Awards.

Finding 3

The department did not accurately report financial activity on the Schedule of Expenditures of Federal Awards for the Special Nutrition Program for Women, Infants and Children (CFDA 10.557) and Childhood Immunization Grants Program (CFDA 93.268).

⁸ State personnel/payroll policy PAY0029.

⁹ Office of the Legislative Auditor's Financial Audit Division Report [08-02, Report on Internal Control Over Statewide Financial Reporting](#), issued February 11, 2008.

The department had the following errors in its Schedule of Expenditures of Federal Awards for these programs:

- The department did not report a materially accurate vaccine value in the Schedule of Expenditures of Federal Awards for the Childhood Immunization Grants Program. The department used inaccurate information that understated the program's adult vaccine value by approximately \$1.2 million. Our inquiry identified the error and resulted in an audit adjustment to the schedule.
- The department frequently used incorrect liability dates when recording payments for services in the state's accounting system. State policy¹⁰ requires all agencies to enter the date goods or services are received so the liability is correctly recorded in the fiscal year it was incurred. Audit testing showed the department often used the invoice or encumbrance date as the date of liability.
- The department did not correctly account for rebate amounts related to the Special Nutrition Program for Women, Infants and Children. The department incorrectly included the \$2.5 million rebate for formula purchased in June of 2007 on the Schedule of Expenditures of Federal Awards for state fiscal year 2008. This \$2.5 million rebate had been correctly reported on the prior state fiscal year Schedule of Expenditures of Federal Awards.

Recommendation

- *The department needs to improve its controls over its Schedule of Expenditures of Federal Awards to ensure that it accurately reports financial activity, including:*
 - *Vaccine values.*
 - *Transaction liability dates.*
 - *Program rebate amounts.*

Finding 4

The Department of Health allowed employees to have incompatible access to the state's accounting system without establishing mitigating controls.

As of January 2009, the department had seven employees with incompatible access to accounts receivable data in the state's accounting system without implementing mitigating controls. This affects the Special Nutrition Program for Women, Infants and Children (CFDA 10.557).

¹⁰ Minnesota Department of Finance Policy Number 0901-01.

State policy¹¹ defines incompatible access and requires separation of incompatible duties so no one employee has control over an entire transaction or process that could result in erroneous or fraudulent transactions. If agencies are unable to adequately separate incompatible duties, the policy requires them to develop and document controls designed to mitigate the risk that error or fraud will not be detected. Since the department was not aware the access was incompatible, it did not have controls designed to mitigate the risk associated with this access.

Recommendation

- *The department needs to ensure it eliminates unnecessary or incompatible access to state business systems. If incompatible access is unavoidable, the department must implement controls designed to mitigate the risk of error or fraud.*

Prior Finding Partially Resolved: The Department of Health did not monitor subrecipient activity, as required by federal regulations.

Finding 5

The department did not review subrecipients' audit reports for the Special Nutrition Program for Women, Infants and Children (CFDA 10.557) and Centers for Disease Control Technical Assistance Program (CFDA 93.283). State policy¹² and Federal regulations¹³ require that subrecipients expending over \$500,000 annually submit an independent audit report within nine months of their year-end to their pass through entity. The department did not obtain audit reports for three of their five subrecipients who met the threshold, nor did the department review audit reports for any of their five subrecipients. The department did not have a process in place to know whether it was fulfilling its subrecipient monitoring responsibilities.

Recommendation

- *The department should comply with federal requirements by obtaining and reviewing subrecipients' audit reports timely and ensuring corrective action on all audit findings.*

¹¹ Minnesota Department of Finance Policy Number 1101-07.

¹² Minnesota Department of Finance Policy Number 0402-03.

¹³ U.S. Office of Management and Budget Circular A-133, Part 3 – Compliance Requirements.

Finding 6

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

Federal requirements prohibit state agencies from awarding assistance to vendors listed as suspended or debarred.¹⁴ Specifically, state agencies must ensure all contracted vendors over \$25,000 are not suspended or debarred. The department could not provide evidence of verification of suspension or debarment for contracts greater than \$25,000 but less than \$100,000. Our audit testing did not identify any suspended or debarred vendors.

Recommendation

- *The Department of Health needs to ensure compliance with federal requirements by verifying suspension and debarment for all federally funded purchases exceeding \$25,000.*

¹⁴ U.S. Office of Management and Budget Circular A-133, Part 3 – Compliance Requirements.



Protecting, maintaining and improving the health of all Minnesotans

March 18, 2009

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

Dear Mr. Nobles:

This letter is prepared in response to the draft audit of certain federal financial assistance programs administered by the Department of Health during state fiscal year 2008.

Recommendation:

The department should regularly review and clearly document its risks, control activities, and internal control monitoring functions for its key business processes.

Response:

The department concurs with this finding and will be working with Minnesota Management and Budget, a work group of agency chief financial officers, and selected department staff to determine the best practices around internal control. Once the best practices are identified, the department will begin to draft policy and procedures on identifying risks and internal controls, working on mitigating procedures as well as training the employees involved in our key business processes.

Recommendation:

The department should provide oversight of its payroll process to ensure compliance with federal and state requirements for documenting time charged to specific programs.

Response:

The department concurs with the finding and, as noted in the audit report, the department developed and implemented a time report system in June of 2008 to be used by all of our federal programs. This system collects actual time that each employee works on a specific program

every two weeks and charges are made to the accounting system based on the distribution of this time. We believe this should eliminate missing time studies and certification as well as reduce or eliminate the need to process manual adjustments in the payroll system.

Recommendation:

The department needs to improve its controls over its Schedule of Expenditures of Federal Awards to ensure that it accurately reports financial activity.

Response:

The department concurs with this finding and, in the future, staff from the department will work more closely with staff from Minnesota Management and Budget (MMB) as well as staff from the Centers for Disease Control to obtain the best numbers available for the financial statements and the time they are prepared. The department will also review the policies issued by MMB on liability dates and provide additional training to the staff responsible for the data entry of these dates.

Recommendation:

The department needs to ensure it eliminates unnecessary or incompatible access to state business systems. If incompatible access is unavoidable, the department must implement controls designed to mitigate the risk of error or fraud.

Response:

The department partially concurs with this finding as steps were in place for the grant specialist to obtain prior approval to enter an accounts receivable write-off from the director of Financial Management. However, based on this recommendation, the department will reassign responsibility among the seven staff so that none of them have access to create an accounts receivable and write-off that same accounts receivable in the system.

Recommendation:

The department should comply with federal requirements by obtaining and reviewing subrecipients' audit reports timely and ensuring corrective action on all audit findings.

Response:

The department concurs with this recommendation and will assign staff to review the list of grantees assigned by MMB to the Department of Health for cognizant agency responsibilities. Once the list is received, this staff will follow-up with those agencies to assure an audit was completed in accordance with the requirements as well as review the audit report for findings.

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Recommendation:

The Department of Health needs to ensure compliance with federal requirements by verifying suspension and debarment for all federally funded purchases exceeding \$25,000.

Response:

The department concurs with the this finding and will work with the Department of Administration, Contract Management, to amend the standard contract language or modify the form currently being used to include a certification from the vendor that the vendor is not on the federal list of suspended or debarred vendors.

I have assigned Craig Acomb, Chief Financial Officer, to implement the activities necessary to comply with these recommendations.

Thank you for the respectful manner in which this audit was conducted.

Sincerely,

/s/ Sanne Magnan

Sanne Magnan, M.D., Ph.D.
Commissioner
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St. Paul, MN 55164-09975